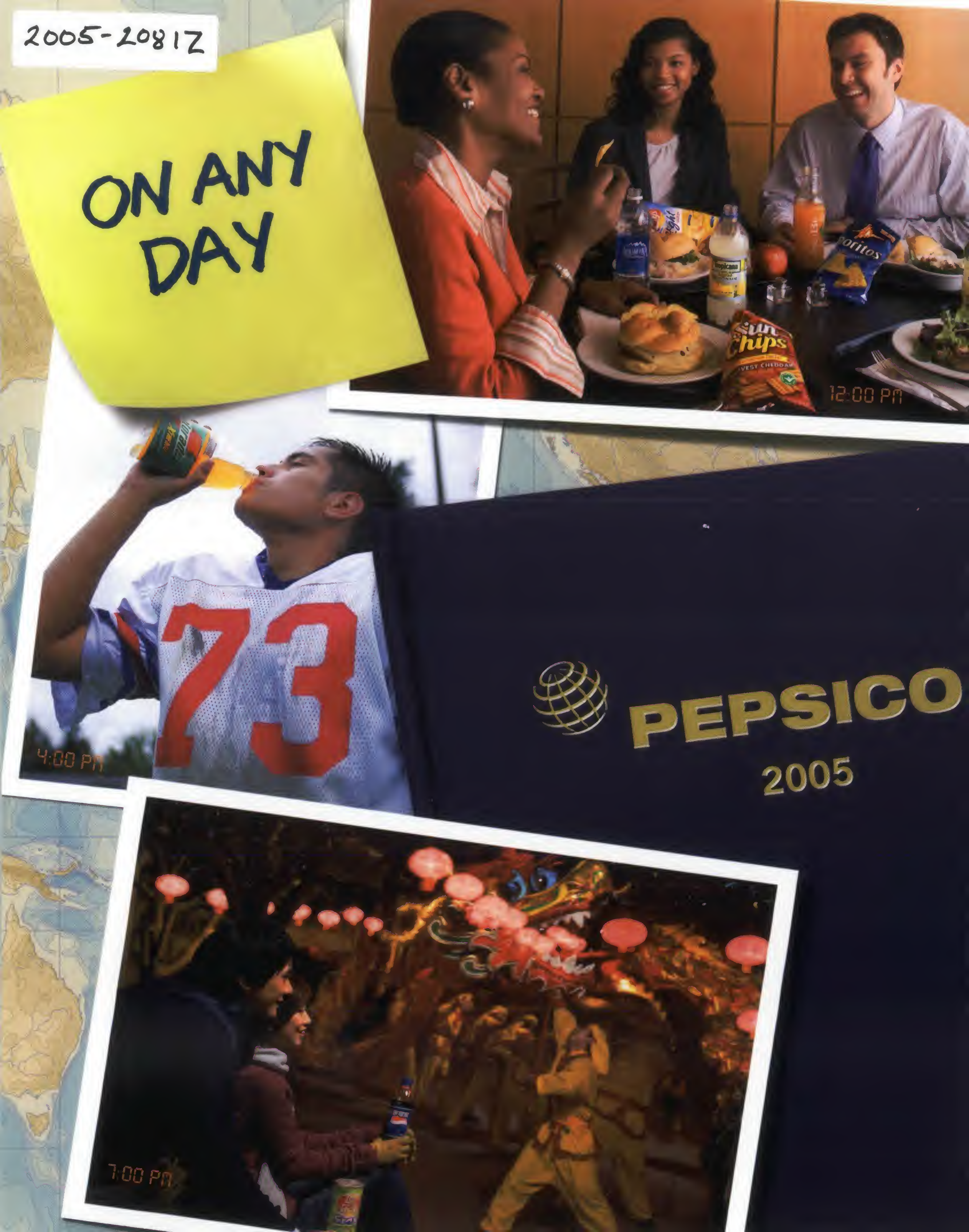
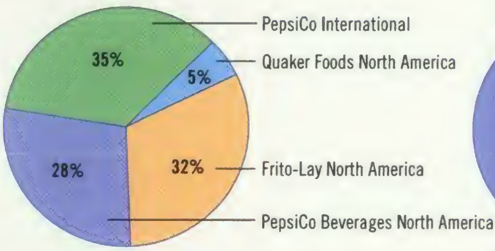

ON ANY DAY
12:00 PM
4:00 PM
PEPSICO
2005
7:00 PM

On any day, around the world, at any moment and in many places, millions of consumers enjoy our brands. Here's how we keep the momentum going.

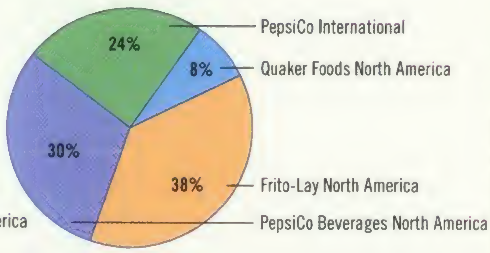
Financial Highlights

PepsiCo, Inc. and Subsidiaries
($ in millions except per share amounts; all per share amounts assume dilution)

Net Revenue
Total: $32,562



Division Operating Profit
Total: $6,710



	2005	2004	% Chg[a]
Summary of Operations			
Total net revenue	**$32,562**	$29,261	11
Division operating profit	**$6,710**	$6,098	10
Total operating profit	**$5,922**	$5,259	13
Net income[b]	**$4,536**	$4,004	13
Earnings per share[b]	**$2.66**	$2.32	15
Other Data			
Management operating cash flow[c]	**$4,204**	$3,705	13
Net cash provided by operating activities	**$5,852**	$5,054	16
Capital spending	**$1,736**	$1,387	25
Common share repurchases	**$3,012**	$3,028	(0.5)
Dividends paid	**$1,642**	$1,329	24
Long-term debt	**$2,313**	$2,397	(3.5)

(a) Percentage changes above and in text are based on unrounded amounts.

(b) In 2005, excludes the impact of AJCA tax charge, the 53rd week and restructuring charges. In 2004, excludes certain prior year tax benefits, and restructuring and impairment charges. See page 76 for reconciliation to net income and earnings per share on a GAAP basis.

(c) Includes the impact of net capital spending. Also, see "Our Liquidity, Capital Resources and Financial Position" in Management's Discussion and Analysis.

Contents

Financial Review

Primary Websites

PepsiCo, Inc. — www.pepsico.com
Frito-Lay North America — www.fritolay.com
Pepsi-Cola North America — www.pepsiworld.com
Tropicana North America — www.tropicana.com
Quaker Foods — www.quakeroats.com
Gatorade — www.gatorade.com
Smart Spot — www.smartspot.com

When market or market share is referred to in this report, the markets and share are defined by the sources of the information, primarily Information Resources, Inc. and ACNielsen. The Measured Channel Information excludes certain customers such as Wal*Mart that do not report data to these services.

PEPSICO

700 Anderson Hill Road
Purchase, New York 10577-1444

March 24, 2006

Dear Fellow PepsiCo Shareholder:

You are invited to attend our Annual Meeting of Shareholders on Wednesday, May 3, 2006 at 9:00 a.m. local time at the headquarters of Frito-Lay, Inc., 7701 Legacy Drive, Plano, Texas.

At the meeting, we will ask you to elect the Board of Directors, to ratify the appointment of the independent registered public accountants, and to consider two shareholder proposals. We will also review the progress of the Company during the past year and answer your questions. The attached Proxy Statement describes the business we will conduct and provides information about the Company that you should consider when you vote your shares.

Cordially,

Steven S Reinemund

PEPSICO

Pepsi Frito-Lay Tropicana Quaker Gatorade

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

PepsiCo will hold its Annual Meeting of Shareholders at the headquarters of Frito-Lay, Inc., 7701 Legacy Drive, Plano, Texas, on Wednesday, **May 3, 2006** at **9:00 a.m.** local time, to:

- Elect the Board of Directors.
- Ratify the appointment of the independent registered public accountants.
- Act upon 2 shareholder proposals described in the attached Proxy Statement.
- Transact any other business that may properly come before the Meeting.

Holders of record of the Company's Common and Convertible Preferred Stock as of the close of business on March 10, 2006 (the "Record Date") will be entitled to vote at the Meeting.

Please refer to the General Information page in this Proxy Statement for additional information about the Annual Meeting and voting.

March 24, 2006

Larry D. Thompson
Secretary

GENERAL INFORMATION ABOUT THE ANNUAL MEETING AND VOTING

Who can attend the Annual Meeting?

Only shareholders of record as of the close of business on March 10, 2006, their authorized representatives and guests will be able to attend the Annual Meeting. Admission will be by ticket only, and those attending the Annual Meeting must bring photo identification. Frito-Lay headquarters is accessible to disabled persons. Upon request, we will provide wireless headsets for hearing amplification.

How do I receive an admission ticket?

If you are a registered shareholder (your shares are held in your name) and plan to attend the Annual Meeting, you can obtain an admission ticket by checking the appropriate box on your proxy card or by contacting PepsiCo's Manager of Shareholder Relations at (914) 253-3055. An admission ticket will then be sent to you.

If you are a beneficial owner (your shares are held in the name of a bank, broker or other holder of record) and plan to attend the Annual Meeting, you can obtain an admission ticket in advance by writing to Investor Relations, PepsiCo, Inc., 700 Anderson Hill Road, Purchase, NY 10577 or by contacting PepsiCo's Manager of Shareholder Relations at (914) 253-3055. Please be sure to include proof of ownership, such as a bank or brokerage account statement. Shareholders who do not obtain tickets in advance may obtain them upon verification of their ownership at the registration desk on the day of the Annual Meeting.

How do I vote at the Annual Meeting?

If you wish to vote at the Annual Meeting, written ballots will be available from the ushers at the meeting. If your shares are held in the name of a bank, broker or other holder of record and you decide to attend and vote at the Annual Meeting, you must obtain a proxy, executed in your favor, from the holder of record to be able to vote at the meeting. However, if you vote by proxy and also attend the meeting, there is no need to vote again at the Annual Meeting unless you wish to change your vote.

How do I vote if I cannot attend the Annual Meeting?

All shareholders who are entitled to vote on the matters that come before the Annual Meeting have the opportunity to do so whether or not they attend the meeting in person. Voting via the Internet or by calling the toll-free number listed on the proxy card will save the Company expense. Instructions for using these convenient services appear on the proxy card. You can also vote your shares by marking your votes on the proxy card, signing and dating it and mailing it promptly using the envelope provided. Proxy votes are tabulated by an independent agent and reported at the Annual Meeting.

- **Registered Shareholders** - If you are a registered shareholder holding shares directly in the Company under your own name and are unable to attend the Annual Meeting, you can vote your shares by proxy in one of the following manners:

  Via Internet at https://www.proxyvotenow.com/pep and following the instructions;
  By Telephone at 1-866-358-4697 in the United States, Canada or Puerto Rico on a touch-tone phone and following the recorded instructions; or
  By Mail by signing and returning the proxy card.

- **Beneficial Owners** - If you are a beneficial owner holding shares through a bank, broker or other holder of record and are unable to attend the Annual Meeting, please refer to the information provided by that entity for instructions on how to vote your shares.

Can I receive proxy materials electronically?

Shareholders can help us reduce the cost of printing and mailing the Proxy Statement and the Annual Report by opting to receive future materials electronically. To enroll, please visit our website at *www.pepsico.com*, click on the "Investors — Shareholder Information — Electronic Delivery Enrollment" links and follow the instructions provided.

Can I revoke my proxy?

You may revoke your proxy by casting a ballot at the Annual Meeting. Any proxy not revoked will be voted as specified on your proxy card. If you return your proxy and no vote is specified (and you do not withhold authority for a nominee or you do not indicate that you abstain), your proxy will be voted in accordance with the Board of Directors' recommendations.

Can employees who participate in PepsiCo's 401(k) plan vote?

Employees who participate in PepsiCo's 401(k) plan (a portion of which constitutes an Employee Stock Ownership Plan (the "ESOP")) can vote the shares held in the 401(k) plan as of the close of business on March 10, 2006. To do so, the employee participant must sign and return a proxy card, or vote via internet or telephone, as instructed in the proxy materials received in connection with the shares in the 401(k) plan. If cards representing shares held in the 401(k) plan are not returned, the 401(k) trustees will not vote those shares for which signed cards are not returned, unless required by law.

What constitutes a quorum at the Annual Meeting?

Under North Carolina law and the Company's By-laws, the presence in person or by proxy of the holders of record of a majority of the votes entitled to be cast constitutes a quorum. Abstentions and broker non-votes are counted as present to determine whether a quorum exists at the meeting.

How are votes counted?

Election of Directors. Under North Carolina law and the Company By-laws, the nominees for directors who receive a majority of all the votes cast shall be elected to the Board of Directors.

Ratification of Independent Registered Public Accountants. Under North Carolina law and the Company By-laws, ratification of the appointment of the independent registered public accountants will be approved if a majority of all the votes cast are in favor of ratification.

Shareholder Proposals. For each of the shareholder proposals, the affirmative vote of a majority of the votes cast is required for adoption of each resolution.

Note on Abstentions. If you abstain from voting on a particular matter, your vote will not be treated as present and, therefore, will not be treated as cast either for or against that proposal.

Note on "Broker Non-Votes." The rules of the New York Stock Exchange determine whether a broker may cast votes related to shares held by the broker for the benefit of the actual owner where the broker does not receive specific voting instructions from the actual owner. On routine matters, such as the Election of Directors or Ratification of Independent Registered Public Accountants, brokers may cast a vote on such shares. On nonroutine matters, such as the Shareholder Proposals, brokers may not vote such shares and these "broker non-votes" will not be treated as present.

Are my votes confidential?

PepsiCo's policy is that proxies identifying individual shareholders are private except as necessary to determine compliance with law or assert or defend legal claims. Proxies may also not be kept confidential in a contested proxy solicitation or in the event that a shareholder makes a written comment on a proxy card or an attachment to it. PepsiCo retains an independent organization to tabulate shareholder votes and certify voting results. The tabulating agent maintains the confidentiality of the proxies throughout the process.

PepsiCo, Inc.
700 Anderson Hill Road
Purchase, New York 10577-1444
www.pepsico.com

March 24, 2006

PROXY STATEMENT

The Board of Directors of PepsiCo, Inc. ("PepsiCo" or the "Company") is soliciting proxies to be voted at the Annual Meeting of Shareholders to be held on Wednesday, May 3, 2006, and at any adjournment of the Meeting. We are sending this Proxy Statement in connection with the proxy solicitation.

PepsiCo's authorized stock includes both Common Stock and Convertible Preferred Stock. As of March 10, 2006, the record date, there were 1,656,106,493 shares of PepsiCo Common Stock outstanding and entitled to one vote each at the Annual Meeting and 349,953 shares of PepsiCo Convertible Preferred Stock outstanding and entitled to 1,736,642 votes at the Annual Meeting, which number is equal to the number of shares of Common Stock into which such shares of Convertible Preferred Stock could be converted on the record date, rounded to the nearest one-tenth. Holders of the Common Stock and the Convertible Preferred Stock vote together on all matters as a single class. The outstanding shares of Common Stock were registered in the names of 196,232 shareholders and the outstanding shares of Convertible Preferred Stock were registered in the names of 2,676 shareholders. As far as we know, no person owns beneficially more than 5% of the outstanding Common or Convertible Preferred Stock.

PepsiCo is making its first mailing of this Proxy Statement on or about March 24, 2006.

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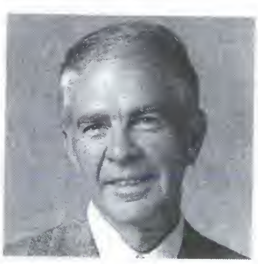
ELECTION OF DIRECTORS (PROXY ITEM NO. 1)

The Board of Directors proposes the following fifteen nominees for election as directors at the Annual Meeting. The directors will hold office from election until the next Annual Meeting of Shareholders, or until their successors are elected and qualified. If any of these nominees for director becomes unavailable, the persons named in the proxy intend to vote for any alternate designated by the current Board of Directors. Proxies cannot be voted for a greater number of persons than the nominees named.

JOHN F. AKERS, 71, former Chairman of the Board and Chief Executive Officer of International Business Machines Corporation, has been a member of PepsiCo's Board since 1991. Mr. Akers joined IBM in 1960 and was Chairman and Chief Executive Officer from 1986 until 1993. He is also a director of Lehman Brothers Holdings Inc., The New York Times Company and W.R. Grace & Co.



ROBERT E. ALLEN, 71, former Chairman of the Board and Chief Executive Officer of AT&T Corp., has been a member of PepsiCo's Board since 1990. He began his career at AT&T in 1957 when he joined Indiana Bell. He was elected President and Chief Operating Officer of AT&T Corp. in 1986, and was Chairman and Chief Executive Officer from 1988 until 1997. He is also a director of Bristol-Myers Squibb Company, and a Trustee of The Mayo Clinic and Wabash College.

DINA DUBLON, 52, was elected a director of PepsiCo in 2005. Ms. Dublon is the former Executive Vice President and Chief Financial Officer, JP Morgan Chase & Co. serving from 1998 until her retirement in September 2004. She is also a director of Microsoft Corp. and Accenture. She is a trustee of Carnegie Mellon University, the Global Fund for Women, the Women's Commission for Refugee Women & Children and GreenStone Media.

VICTOR J. DZAU, MD, 60, was elected a director of PepsiCo in 2005. Dr. Dzau is chancellor for health affairs at Duke University and President and CEO of the Duke University Health System since July 2004. Prior to that he served as Hershey Professor of Medicine at Harvard Medical School and Chairman of the Department of Medicine at Brigham and Women's Hospital in Boston Massachusetts from 1996 to 2004. He is a member of the Institute of Medicine of the National Academy of Sciences and the European Academy of Science and Arts. He was the previous Chairman of the National Institutes of Health (NIH) Cardiovascular Disease Advisory Committee, he served on the Advisory Committee of the Director of NIH. Dr. Dzau has been named 2004 Distinguished Scientist of the American Heart Association and was the recipient of the 2004 Max Delbruck Medal from the Max Delbruck Medical Center for Molecular Medicine, Berlin, Germany and the 2005 Ellis Island Medal of honor.

RAY L. HUNT, 62, Chief Executive Officer of Hunt Oil Company and Chairman, Chief Executive Officer and President, Hunt Consolidated, Inc., was elected to PepsiCo's Board in 1996. Mr. Hunt began his association with Hunt Oil Company in 1958 and has held his current position since 1976. He is also a director of Halliburton Company, Electronic Data Systems Corporation, King Ranch, Inc., Verde Group, LLC and Chairman of the Board of Directors of the Federal Reserve Bank of Dallas.

ALBERTO IBARGÜEN, 62, was elected as a director of PepsiCo in 2005. Mr. Ibargüen is President and Chief Executive Officer of the John S. and James L. Knight Foundation. Mr. Ibargüen previously served as Chairman of Miami Herald Publishing Co., a Knight Ridder subsidiary, and as publisher of *The Miami Herald* and *El Nuevo* Herald. He is a member of the board of Newseum, a member of the Trustees' Council of the National Gallery of Art, and is on the Advisory Council of the Public Company Accounting Oversight Board.

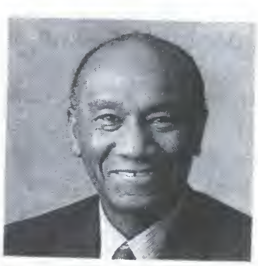
ARTHUR C. MARTINEZ, 66, former Chairman of the Board, President and Chief Executive Officer of Sears, Roebuck and Co., was elected to PepsiCo's Board in 1999. Mr. Martinez was Chairman and Chief Executive Officer of the former Sears Merchandise Group from 1992 to 1995 and served as Chairman of the Board, President and Chief Executive Officer of Sears, Roebuck and Co. from 1995 until 2000. He served as Vice Chairman and a director of Saks Fifth Avenue from 1990 to 1992. He is also a director of Liz Claiborne, Inc., International Flavors & Fragrances Inc. and IAC/ Interactive Corp. Mr. Martinez is Deputy Chairman of the Supervisory Board of ABN AMRO Holding, N.V.

INDRA K. NOOYI, 50, was elected to PepsiCo's Board and became President and Chief Financial Officer in May 2001, after serving as Senior Vice President and Chief Financial Officer since February 2000. Ms. Nooyi also served as Senior Vice President, Strategic Planning and Senior Vice President, Corporate Strategy and Development from 1994 until 2000. Prior to joining PepsiCo, Ms. Nooyi spent four years as Senior Vice President of Strategy, Planning and Strategic Marketing for Asea Brown Boveri, Inc. She was also Vice President and Director of Corporate Strategy and Planning at Motorola, Inc. Ms. Nooyi is also a director of Motorola, Inc.

STEVEN S REINEMUND, 57, has been PepsiCo's Chairman and Chief Executive Officer since May 2001. He was elected a director of PepsiCo in 1996 and before assuming his current position, served as President and Chief Operating Officer from September 1999 until May 2001. Mr. Reinemund began his career with PepsiCo in 1984 as a senior operating officer of Pizza Hut, Inc. He became President and Chief Executive Officer of Pizza Hut in 1986, and President and Chief Executive Officer of Pizza Hut Worldwide in 1991. In 1992, Mr. Reinemund became President and Chief Executive Officer of Frito-Lay, Inc., and Chairman and Chief Executive Officer of the Frito-Lay Company in 1996. Mr. Reinemund is also a director of Johnson & Johnson.

SHARON PERCY ROCKEFELLER, 61, was elected a director of PepsiCo in 1986. She is President and Chief Executive Officer of WETA public stations in Washington, D.C., a position she has held since 1989, and was a member of the Board of Directors of WETA from 1985 to 1989. She was a member of the Board of Directors of the Corporation for Public Broadcasting until 1992 and the Board of Directors of Public Broadcasting Service, Washington, D.C., until 2003.

JAMES J. SCHIRO, 60, was elected to PepsiCo's Board in January 2003. Mr. Schiro became Chief Executive Officer of Zurich Financial Services in May 2002, after serving as Chief Operating Officer – Group Finance since March 2002. He joined Price Waterhouse in 1967, where he held various management positions. In 1994 he was elected Chairman and senior partner of Price Waterhouse, and in 1998 became Chief Executive Officer of PricewaterhouseCoopers, after the merger of Price Waterhouse and Coopers & Lybrand. Mr. Schiro is also a director of Royal Philips Electronics.



FRANKLIN A. THOMAS, 71, was elected to PepsiCo's Board in 1994. From 1967 to 1977, he was President and Chief Executive Officer of the Bedford-Stuyvesant Restoration Corporation. From 1977 to 1979 Mr. Thomas had a private law practice in New York City. Mr. Thomas was President of the Ford Foundation from 1979 to April 1996 and is currently a consultant to the TFF Study Group, a non-profit organization assisting development in southern Africa. He is also a director of ALCOA Inc., Citigroup Inc., and Lucent Technologies Inc.

CYNTHIA M. TRUDELL, 52, was elected to PepsiCo's Board in January 2000. From 2001 to 2006, Ms. Trudell was President of Sea Ray Group. From 1999 until 2001, Ms. Trudell served as General Motors' Vice President, and Chairman and President of Saturn Corporation, a wholly owned subsidiary of GM. Ms. Trudell began her career with the Ford Motor Co. as a chemical process engineer. In 1981, she joined GM and held various engineering and manufacturing supervisory positions. In 1995, she became plant manager at GM's Wilmington Assembly Center in Delaware. In 1996, she became President of IBC Vehicles in Luton, England, a joint venture between General Motors and Isuzu. Ms. Trudell is also a director of Canadian Imperial Bank of Commerce (CIBC).

DANIEL VASELLA, 52, was elected to PepsiCo's Board in February 2002. Dr. Vasella became Chairman of the Board and Chief Executive Officer of Novartis AG in 1999, after serving as President since 1996. From 1992 to 1996, Dr. Vasella held the positions of Chief Executive Officer, Chief Operating Officer, Senior Vice President and Head of Worldwide Development and Head of Corporate Marketing at Sandoz Pharma Ltd. He also served at Sandoz Pharmaceuticals Corporation from 1988 to 1992.

MICHAEL D. WHITE, 54, was elected to PepsiCo's Board and named Vice Chairman of PepsiCo in March 2006. He continues to serve as Chairman and Chief Executive Officer of PepsiCo International, a position he has held since February 2003. From 2000 to 2003, he served as President and Chief Executive Officer of Frito-Lay's Europe/Africa/Middle East division. From 1998 to 2000, Mr. White was Senior Vice President and Chief Financial Officer of PepsiCo. Mr. White has also served as Executive Vice President and Chief Financial Officer of PepsiCo Foods International and Chief Financial Officer of Frito-Lay North America. He joined Frito-Lay in 1990 as Vice President of Planning. Mr. White is also a director of Whirlpool Corporation.

OWNERSHIP OF PEPSICO COMMON STOCK BY DIRECTORS AND EXECUTIVE OFFICERS

The following table shows, as of March 10, 2006, the shares of PepsiCo Common Stock beneficially owned by each director (including each nominee), by each of our five most highly compensated executive officers, and by all directors and all executive officers as a group:

Name of Individual or Group	Number of Shares of PepsiCo Common Stock Beneficially Owned(1)
John F. Akers	88,083
Robert E. Allen	50,494
John C. Compton	704,218
Dina Dublon	1,000
Victor J. Dzau	1,000
Ray L. Hunt (2)	531,897
Alberto Ibargüen	1,000
Arthur C. Martinez	25,645
Indra K. Nooyi	906,725
Steven S Reinemund (2)	3,692,313
Sharon Percy Rockefeller	64,734
Irene B. Rosenfeld	13,631
James J. Schiro	12,462
Franklin A. Thomas	40,244
Cynthia M. Trudell	26,866
Daniel Vasella	15,584
Michael D. White	1,144,951
All directors and executive officers as a group (23 persons)	9,474,437

(1) The shares shown include the following shares that directors and executive officers have the right to acquire within 60 days after March 10, 2006 through the exercise of vested stock options: John F. Akers, 63,072 shares; Robert E. Allen, 43,358 shares; John C. Compton, 686,320 shares; Ray L. Hunt, 62,272 shares; Arthur C. Martinez, 23,645 shares; Indra K. Nooyi, 892,512 shares; Steven S Reinemund, 3,581,261 shares; Sharon Percy Rockefeller, 34,869 shares; James J. Schiro, 10,377 shares; Franklin A. Thomas, 39,244 shares; Cynthia M. Trudell, 26,866 shares; Daniel Vasella, 10,417 shares; Michael D. White, 1,105,240 shares; and all directors and executive officers as a group, 8,649,916 shares.

(2) The shares shown for Mr. Hunt include (i) 26,700 shares held in a corporation over which Mr. Hunt has sole voting and investment power, (ii) 262,286 shares held in trusts over which Mr. Hunt has shared voting power and sole investment power, and (iii) 152,500 shares held in a trust over which Mr. Hunt has sole voting power and no investment power. The shares shown for Mr. Reinemund include 103,631 shares over which Mr. Reinemund shares voting and investment power with his spouse.

The following table shows, as of March 10, 2006 the number of PepsiCo Common Stock equivalents held in the PepsiCo deferred income program by each director (including each nominee), by each of our five most highly compensated executive officers, and by all directors and all executive officers as a group:

Name of Individual or Group	Number of PepsiCo Common Stock Equivalents Held in PepsiCo's Deferred Income Program
John F. Akers	6,914
Robert E. Allen	15,369
John C. Compton	22,712
Dina Dublon	460
Victor J. Dzau	2,237
Ray L. Hunt	11,197
Alberto Ibargüen	1,777
Arthur C. Martinez	15,961
Indra K. Nooyi	50,510
Steven S Reinemund	238,417
Sharon Percy Rockefeller	0
Irene B. Rosenfeld	0
James J. Schiro	3,879
Franklin A. Thomas	12,142
Cynthia M. Trudell	9,673
Daniel Vasella	0
Michael D. White	0
All directors and executive officers as a group (23 persons)	391,248

Directors and executive officers as a group own less than 1% of outstanding PepsiCo Common Stock. No directors or executive officers own any PepsiCo Convertible Preferred Stock.

CORPORATE GOVERNANCE AT PEPSICO

Board of Directors

Our business and affairs are overseen by our Board of Directors pursuant to the North Carolina Business Corporation Act and our By-Laws. Members of the Board of Directors are kept informed of the Company's business through discussions with the Chairman and Chief Executive Officer, and with key members of management, by reviewing materials provided to them and by participating in Board and Committee meetings. Members of the Board of Directors are elected annually.

Regular attendance at Board meetings is required of each director. PepsiCo's Board held six meetings during 2005. Average attendance by incumbent directors at Board and standing Committee meetings was 97%. No incumbent director attended fewer than 75% of the total number of Board and standing Committee meetings. The non-employee directors met in executive session at all six Board meetings in 2005. All directors attended the 2005 Annual Meeting, except for the three directors who joined the Board following the Annual Meeting and one additional director.

In 2002, the Board of Directors adopted Corporate Governance Guidelines. These Guidelines were amended in 2005 in accordance with the revised New York Stock Exchange Listing Standards and rules adopted by the Securities and Exchange Commission. The Guidelines were also amended in 2006 and the revised Guidelines are attached to this Proxy Statement as Exhibit A and are also available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section and are available in print to any shareholder who requests a copy. The Company's Worldwide Code of Conduct is also available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section and is available in print to any shareholder who requests a copy. Annually, all of PepsiCo's executive officers, other senior employees and directors sign certifications with respect to their compliance with the Company's Worldwide Code of Conduct.

Director Independence

The Board of Directors has determined that the following non-employee directors standing for election have met the independence standards within the meaning of the rules of the New York Stock Exchange, based on the application of the Company's categorical independence standards that were recommended by the Nominating and Corporate Governance Committee and adopted by the Board of Directors, as detailed in the Corporate Governance Guidelines attached as Exhibit A to this Proxy Statement:

John F. Akers	Ray L. Hunt	James J. Schiro
Robert E. Allen	Alberto Ibargüen	Franklin A. Thomas
Dina Dublon	Arthur C. Martinez	Cynthia M. Trudell
Victor J. Dzau	Sharon Percy Rockefeller	Daniel Vasella

None of the non-employee directors receive any fees from the Company other than those received in his or her capacity as a director.

Presiding Director

In September 2002, the Board of Directors appointed Robert E. Allen as the Presiding Director of the Board. In his capacity as the Presiding Director, Mr. Allen presides at the regularly-scheduled executive sessions of the Board, at which only non-employee directors are present. He also advises the Chairman of the Board and, as appropriate, Committee chairs with respect to agendas and information needs relating to the Board and Committee meetings, and performs other duties that the Board may from time to time delegate to assist the Board in the fulfillment of its responsibilities. Shareholders may communicate with Mr. Allen by sending a letter addressed to PepsiCo, Inc., 700 Anderson Hill Road, Purchase, New York, 10577, Attention: Presiding Director, or by utilizing one of the means through which the Board may be contacted, as provided at www.pepsico.com under "Contact."

Communications to the Board of Directors

The Board of Directors has established a process for contacting the Board, a committee of the Board or an individual member of the Board. The means through which the Board may be contacted are provided at www.pepsico.com under Corporate Governance in the "Investors" section. The PepsiCo Corporate Law Department reviews all communications sent to the Board of Directors relating to the duties and responsibilities of the Board and its committees. The Corporate Law Department maintains a log of all such communications and regularly provides a summary of communications to the Board that relate to the functions of the Board or a Board committee or that otherwise require Board attention. Directors may at any time review the log of Board communications received by the Company and request copies or summaries of such communications. In addition, the Corporate Law Department may forward certain communications only to the Presiding Director, the Chair of the relevant committee or the individual Board member to whom a communication is directed. Concerns relating to PepsiCo's accounting, internal accounting controls or auditing matters will be referred directly to members of the Audit Committee.

Exercise and Hold Policy and Stock Ownership Guidelines

To ensure that our senior executives exhibit a strong commitment to PepsiCo share ownership, the Board of Directors adopted an Exercise and Hold Policy and Stock Ownership Guidelines that apply to all directors and certain senior executives of the Company. Under the Exercise and Hold Policy, the aggregate amount of cash that may be received by an individual upon the exercise of stock options during each calendar year is limited to 20% of the pre-tax gains on all vested outstanding options as of February 1 of that year. Amounts in excess of the 20% limit must be held in PepsiCo shares for at least one year after exercise. Under the Company's Stock Ownership Guidelines, certain senior executives and directors are required to own PepsiCo stock worth between two times and eight times base compensation, depending on their position.

Political Contributions Policy

In 2005, the Board of Directors adopted a Political Contributions Policy for the Company, which can be found on the website at *www.pepsico.com* in the "Investors" section under "Corporate Governance – Policies." The Political Contributions Policy, together with other policies and procedures, including the Company's Code of Conduct, guide the Company's approach to political contributions. In connection with the development of this policy and in keeping with the Company's goals of transparency, the Company's annual political contributions will now be posted on our website, starting in April 2006.

Committees of the Board of Directors

The Board of Directors has three standing committees: Audit, Compensation, and Nominating and Corporate Governance. The table below indicates the members of each Board committee standing for re-election:

Name	Nominating and Corporate Governance	Compensation	Audit
John F. Akers	X	Chair	
Robert E. Allen[1]	X	X	
Dina Dublon			X
Victor J. Dzau	X	X	
Ray L. Hunt	Chair[2]	X	
Alberto Ibargüen			X
Arthur C. Martinez	X[3]	X	
Indra K. Nooyi			
Steven S Reinemund			
Sharon P. Rockefeller	X	X	
James J. Schiro			Chair[4]
Franklin A. Thomas			X
Cynthia M. Trudell			X
Daniel Vasella	X	X	
Michael D. White			

1 Mr. Allen is the Presiding Director of our Board.
2 Effective May 3, 2006, Mr. Hunt will be Chairman of the Nominating and Corporate Governance Committee. Mr. Allen was the Committee's previous Chairman.
3 Effective 3, 2006, Arthur C. Martinez will no longer be a member of the Audit Committee and will become a member of the Nominating and Corporate Governance and Compensation Committees.
4 Effective May 3, 2006, Mr. Schiro will be Chairman of the Audit Committee. Mr. Martinez was the Committee's previous Chairman.

The Nominating and Corporate Governance Committee

The Nominating and Corporate Governance Committee, which was established in 1997 and renamed in 2002, held five meetings in 2005. The Nominating and Corporate Governance Committee: (a) identifies and recommends to the Board for election and/or appointment qualified candidates for membership on the Board and the committees of the Board; (b) develops and recommends to the Board corporate governance principles and the Worldwide Code of Conduct applicable to the Company and monitors compliance with all such principles and policies; (c) develops and recommends to the Board criteria to assess the independence of members of the Board; (d) makes recommendations to the Board concerning the composition, size, structure and activities of the Board and its committees; (e) assesses and reports to the Board on the performance and effectiveness of the Board and its committees; and (f) reviews and reports to the Board with respect to director compensation and benefits. The Nominating and Corporate Governance Committee Charter is available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section and is also available in print to any shareholder who requests a copy. The Nominating and Corporate Governance Committee is comprised entirely of directors who meet the independence requirements of the New York Stock Exchange and applicable securities laws.

Director Nomination Process

The Nominating and Corporate Governance Committee does not solicit director nominations, but will consider recommendations for director nominees made by shareholders, if the individuals recommended meet certain minimum Board membership criteria. As set forth in the Company's Corporate Governance Guidelines (attached as Exhibit A), when seeking candidates for the Board of Directors, the Nominating and Corporate Governance Committee will generally look for individuals who have displayed high ethical standards and sound business judgment. The Committee's assessment of Board candidates also includes consideration of: (i) relevant knowledge and diversity of background and experience in areas including business, finance and accounting, technology, marketing, international business and government; (ii) personal qualities of leadership, character, judgment and whether the candidate possesses a reputation in the community at large of integrity, trust, respect, competence and adherence to the highest ethical standards; (iii) roles and contributions valuable to the business community and (iv) whether the candidate is free of conflicts and has the time required for preparation, participation and attendance at all meetings. Shareholder recommendations should be sent to the Secretary of PepsiCo at 700 Anderson Hill Road, Purchase, New York 10577 and must include detailed background regarding the suggested candidate that demonstrates how the individual meets the minimum Board membership criteria described above.

Nominations received by the Secretary of the Company from shareholders are reviewed by the Chairman of the Nominating and Corporate Governance Committee to determine whether the candidate possesses the minimum qualifications described above, and if so, whether the candidate's expertise and particular set of skills and background fit the current needs of the Board. If the candidate meets the requirements for a current vacancy on the Board, the submission materials are reviewed with the Nominating and Corporate Governance Committee and are responded to by the Chairman of the Committee or his designee.

The process of reviewing and evaluating candidates submitted by shareholders is designed to ensure that the Board includes members with diverse backgrounds, skills and experience, including appropriate financial and other expertise relevant to the business of the Company. The process for evaluation of candidates submitted by non-shareholders of the Company is handled similarly.

From time to time, the Nominating and Corporate Governance Committee engages consulting firms to perform searches for director candidates who meet the current needs of the Board. If a consulting firm is retained to assist in the search process for a director, a fee is paid to such firm.

The Audit Committee

The Audit Committee, which was established in 1967, held nine meetings in 2005. The Audit Committee's primary responsibilities are to assist the Board's oversight of: (a) the quality and integrity of the Company's financial statements and its related internal controls over financial reporting; (b) the Company's compliance with legal and regulatory requirements; (c) the independent auditor's qualifications and independence; and (d) the performance of the Company's internal audit function and the independent auditors. The report of the Audit Committee is set forth on page 11 of this Proxy Statement. The Audit Committee Charter is available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section and is also available in print to any shareholder who requests a copy.

Financial Expertise and Financial Literacy

The Board of Directors has determined that Dina Dublon and James J. Schiro, members of our Audit Committee, satisfy the criteria adopted by the Securities and Exchange Commission to serve as "audit committee financial experts" and are independent directors, pursuant to the standards set forth in the Company's Corporate Governance Guidelines and the requirements under the Securities Exchange Act of 1934 and the New York Stock Exchange Listing Standards. In addition, the Board of Directors has determined that Dina Dublon, Alberto Ibargüen, James J. Schiro, Franklin A. Thomas and Cynthia M. Trudell, all members of our Audit Committee, and Arthur C. Martinez, are independent directors and are financially literate within the meaning of the New York Stock Exchange Listing Standards.

Directors on Multiple Audit Committees

None of the Company's directors serve on the audit committee of more than three public companies.

The Compensation Committee

The Compensation Committee, which has been active since 1955, held three meetings during 2005. The Compensation Committee: (a) oversees the policies of the Company relating to compensation of the Company's executives and makes recommendations to the Board with respect to such policies; (b) produces a report on executive compensation for inclusion in the Company's Proxy Statement; and (c) monitors the development and implementation of succession plans for the Chief Executive Officer and other key executives, and makes recommendations to the Board with respect to such plans. The Compensation Committee report on executive compensation is set forth on page [14] of this Proxy Statement. The Compensation Committee Charter is available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section and is also available in print to any shareholder who requests a copy.

Compensation Committee Interlocks and Insider Participation

None of PepsiCo's independent directors is an executive officer of a public company of which a PepsiCo executive officer is a director.

AUDIT COMMITTEE REPORT

PepsiCo's Audit Committee reports to and acts on behalf of the Board of Directors by providing oversight of the Company's independent auditors and the Company's financial management and financial reporting procedures. The Audit Committee is comprised entirely of directors who meet the independence, financial experience and other qualification requirements of the New York Stock Exchange and applicable securities laws. The Audit Committee operates under a written charter adopted by the Board of Directors, which is reviewed annually and is available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section.

The Company's management has responsibility for preparing the Company's financial statements and the Company's independent auditors (independent registered public accountant) KPMG LLP ("KPMG"), is responsible for auditing those financial statements. In this context, the Audit Committee has met with management and KPMG to review and discuss the Company's audited financial statements. The Audit Committee discussed with Company management the critical accounting policies applied by the Company in the preparation of its financial statements. These policies arise in conjunction with: revenue recognition; brand and goodwill valuations; income tax expense and accruals; stock-based compensation expense; and pension and retiree medical plans. The Company's management has represented to the Audit Committee that the financial statements were prepared in accordance with generally accepted accounting principles. The Audit Committee discussed with KPMG the matters required to be discussed by the Statement on Auditing Standards No. 61 (Communications with Audit Committees) and the Sarbanes-Oxley Act of 2002, and had the opportunity to ask KPMG questions relating to such matters. The discussions included the quality, and not just the acceptability, of the accounting principles utilized, the reasonableness of significant accounting judgments, and the clarity of disclosures in the financial statements. The Audit Committee also discussed with Company management the process for certifications by the Company's Chief Executive Officer and Chief Financial Officer, which is required by the Securities and Exchange Commission and the Sarbanes-Oxley Act of 2002 for certain of the Company's filings with the Securities and Exchange Commission.

The Audit Committee reviewed with the Company's internal and independent auditors the overall scope and plans for their respective audits for 2005. The Audit Committee also received regular updates from the Company's General Auditor on internal control and business risks and the

Company's senior officer for compliance and business practices on compliance issues. The Audit Committee meets with the internal and independent auditors, with and without management present, to discuss their evaluations of the Company's internal controls and the overall quality of the Company's financial reporting. The Audit Committee also meets with the Company's General Counsel, with and without management present, to discuss the Company's compliance with laws and regulations.

The Audit Committee reviewed and discussed with KPMG, KPMG's independence and, as part of that review, received the written disclosures and letter required by Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees) and by all relevant professional and regulatory standards relating to KPMG's independence from the Company. The Audit Committee also reviewed and pre-approved all fees paid to the independent auditors. These fees are described in the next section of this Proxy Statement. The Audit Committee also considered whether KPMG's provision of non-audit services to the Company was compatible with the auditor's independence. The Committee has adopted a formal policy on Audit, Audit-Related and Non-Audit Services, which is published on the Company's website and which is briefly described in the next section of this Proxy Statement. The Audit Committee concluded that the independent auditor is independent from the Company and its management.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors, and the Board has approved, that the audited financial statements be included in the Annual Report on Form 10-K for the fiscal year ended December 31, 2005, for filing with the Securities and Exchange Commission. The Audit Committee has also retained KPMG as the Company's independent auditors for the fiscal year 2006, and the Audit Committee and the Board have recommended that shareholders ratify the appointment of KPMG as the Company's independent auditors for the fiscal year 2006.

Dina Dublon and Alberto Ibargüen commenced service on the Audit Committee on September 16, 2005 and November 18, 2005, respectively. Effective May 3, 2006, Arthur C. Martinez will no longer be a member of the Audit Committee and will become a member of the Company's Compensation and Nominating and Corporate Governance Committees. James J. Schiro will become the new Chairman of the Audit Committee.

THE AUDIT COMMITTEE

DINA DUBLON
ALBERTO IBARGÜEN
ARTHUR C. MARTINEZ, CHAIRMAN
JAMES J. SCHIRO
FRANKLIN A. THOMAS
CYNTHIA M. TRUDELL

AUDIT AND NON-AUDIT FEES

The following table presents fees for professional audit services rendered by KPMG LLP, the Company's independent auditor, for the audit of the Company's annual financial statements for 2004 and 2005, and fees billed for other services rendered by KPMG LLP.

	2004	2005
Audit fees	$18,589,000	$16,550,000
Audit-related fees (1)	$ 3,714,000	$ 1,727,000
Tax fees (2)	$ 1,165,000	$ 887,000
All other fees	$ 0	$ 0

(1) Audit-related fees for 2004 and 2005 consisted primarily of the audits of certain employee benefit plans, due diligence reviews of certain businesses acquired, and internal control reviews. The decrease in 2005 fees was primarily related to services provided in 2004 in connection with Section 404 of the Sarbanes-Oxley Act of 2002, which did not recur in 2005.

(2) Tax fees for 2004 and 2005 consisted primarily of international tax compliance services.

We understand the need for the independent auditors to maintain their objectivity and independence, both in appearance and in fact, in their audit of the Company's financial statements. Accordingly, the Audit Committee has adopted the PepsiCo Policy for Audit, Audit-Related and Non-Audit Services. The Policy provides that the Audit Committee will engage the auditor for the audit of the Company's consolidated financial statements and other audit-related work. The auditor may also be engaged for tax and other non-audit related work if those services: enhance and support the attest function of the audit; are an extension to the audit or audit-related services; or are services with respect to which, under the circumstances, KPMG offers unique qualification and there is clearly no question regarding their independence in providing such service. The policy further provides that on an annual basis the auditor's Global Lead Audit Partner will review with the Audit Committee the services the auditor expects to provide in the coming year and the related fee estimates. In addition, PepsiCo will provide the Audit Committee with a quarterly status report regarding the Committee's pre-approval of audit related, tax or other non-audit services that the auditor has been pre-approved to perform, has been asked to provide or may be expected to provide in the following quarter. PepsiCo's Policy for Audit, Audit-Related and Non-Audit Services is available on the Company's website at www.pepsico.com under Corporate Governance in the "Investors" section.

DIRECTORS' COMPENSATION

The Nominating and Corporate Governance Committee reviewed the compensation program for directors in consultation with independent advisors who report directly to the Committee. In order to maintain the market competitiveness of the program, the Nominating and Corporate Governance Committee recommended, and the Board approved, certain changes to the programs described below, for the 2006 period (covering October 2005 through September 2006). The previous program had been unchanged since 2003.

Directors who are employees of the Company receive no additional pay for serving as directors. All other directors receive an annual retainer of $100,000 and an annual equity award. Committee chairs receive an additional $20,000 retainer for the supplemental duties associated with serving as a committee chair. Directors do not receive any meeting fees. All newly appointed directors receive a one-time grant of 1,000 shares of PepsiCo Common Stock when they join the Board. The annual retainer ($100,000), the Board and committee per meeting fee ($0) and the equity grant to newly appointed directors (1,000 shares) remain unchanged from the 2005 period (covering October 2004 through September 2005). The committee chair retainer was increased from $10,000 in the 2005 period to $20,000 in the 2006 period in response to changes in the marketplace.

Directors are reimbursed for expenses incurred to attend Board and committee meetings. Directors do not have a retirement plan, nor do they receive any benefits such as life or medical insurance. Directors do receive business travel and accident coverage and are eligible for PepsiCo Foundation matching of charitable contributions.

Directors may elect to receive their retainer in cash or defer their retainer into PepsiCo Common Stock equivalents, which are payable in cash at the end of the deferral period.

The value of the annual equity award to directors for the 2006 period is $100,000. This amount is equally split between stock options and restricted stock units to deliver a balanced program and to maintain consistency with the equity mix granted to senior executives. The number of restricted stock units awarded is determined by dividing $50,000 by the fair market value of PepsiCo Stock on the date of grant (October 1 in 2005). The number of stock options is determined by multiplying the number of restricted stock units granted by four. In the 2005 period, the annual equity award value was $75,000, which was comprised of restricted stock units, stock options, or a combination of both, as elected by each director and calculated in the same manner as the October 1, 2005 grant. Restricted stock units and stock options normally vest after three years and vest earlier in the case of the director's death, disability or retirement. Stock options granted have an exercise price equal to the fair market value of PepsiCo Common Stock on the date of grant.

EXECUTIVE COMPENSATION

COMPENSATION COMMITTEE REPORT ON EXECUTIVE COMPENSATION

The Compensation Committee (the "Committee") is composed entirely of independent members of the Board. The Committee oversees PepsiCo's compensation and stock-based programs and establishes the principles and strategies that guide the design of compensation plans and benefit programs for all employees within PepsiCo. The Committee makes recommendations to the Board regarding the compensation of PepsiCo's executive officers. The Board approves all compensation actions regarding the Chief Executive Officer ("CEO") and all other executive officers.

The Committee continuously evaluates PepsiCo's plans and programs against current and emerging competitive practices, legal and regulatory developments, and corporate governance trends. Utilizing input from independent outside advisors that report directly to the Committee, the Committee evaluates PepsiCo's financial performance relative to peer companies and reviews data showing all components of compensation and benefits provided to the executive officers. In 2005, the review provided assurance that PepsiCo's executive compensation was appropriately aligned with PepsiCo's financial performance, and that the programs should continue to support the attraction and retention of talent necessary to maintain the long history of strong sales growth, profitability and shareholder returns.

Compensation Philosophy

Our philosophy is that PepsiCo will achieve its best results if its employees act and are rewarded as business owners. Ownership is not only about owning stock, but is also about being accountable for business results, in good times and bad. Owners act with the conviction that their business is personal and that they can make a difference. Owners take initiative and they take responsibility for the assets of the business, including its employees. As executives progress to higher levels at PepsiCo, their responsibilities, risks and rewards will progress as well.

The Committee recognizes that PepsiCo's compensation programs are required to help recruit, retain and motivate a large group of talented and diverse domestic and international employees. The Committee assures that the programs are incentive based, competitive in the marketplace and that there is a significant weighting of Company performance when determining total compensation.

Towards these ends, the Committee works with outside independent advisors to determine PepsiCo's financial performance relative to peer companies and strongly considers this when granting compensation to the CEO, other executive officers and all PepsiCo employees. As a result, when PepsiCo's financial performance is above the median (i.e. third quartile performance) of peer companies, total compensation is delivered above the median (i.e. third quartile compensation). Likewise if PepsiCo's financial performance were to be below the median of peer companies, total compensation would be delivered below the median.

Annually, the Committee:

- Approves performance targets based on the achievement of specific performance goals, which are either Company or business unit focused depending on the executive officer's position and scope of responsibility.
- Ensures that a significant portion of the total compensation package for the CEO, executive officers and other executives are performance-based and that compensation opportunities are designed to create incentives for above-target performance and consequences for below target performance.
- Reviews overall corporate performance and compensation levels against a survey of leading consumer product companies and against surveys of a broader range of major companies,

including the Fortune 100. As a part of this work, independent advisors validate that total compensation paid is appropriate based on an analysis that compares PepsiCo's performance to the performance of the peer group using publicly available financial performance measures including long-term shareholder returns over one and three year time periods.

- Approves annual and long-term incentive awards for the year based on performance achieved in the prior year relative to the pre-approved targets. In determining the final awards, the Committee considers objective data concerning PepsiCo's financial performance, including sales volume, revenue, operating profit, cash flow, capital returns and earnings per share. The Committee also considers other strategic achievements, such as improved operating efficiencies, customer and employee satisfaction and talent development.

Stock Ownership and Hold Policy

To reinforce the Company's ownership philosophy, senior executives are required to own multiples of their salary in PepsiCo stock under the Board approved stock ownership guidelines.

The ownership guidelines operate along with a policy that limits annual option exercises for cash to 20% of vested gains. Any proceeds in excess of this 20% limit must be held in PepsiCo shares for at least one year after the date of exercise.

Specific Compensation Programs

For 2005, the primary components of PepsiCo's compensation program for executive officers were base salary, annual incentives, and long-term incentive awards. Executive officers also participated in PepsiCo's qualified and nonqualified employee benefit plans. These plans are designed to provide retirement income and are the same as those generally available to other employees. Executive officers, including the CEO, do not have employment contracts.

It is the Committee's intention that substantially all executive compensation be fully deductible for federal income tax purposes. Thus, the Committee ensured that the compensation decisions relating to executive officers were made with full consideration of the implications of Internal Revenue Code Section 162(m). Executive officers can defer base salary and annual incentives, subject to applicable law.

Base Salary. The relative levels of base salary for the CEO and the other executive officers are based on the underlying accountabilities of each executive's position and reflect each executive officer's scope of responsibility. The salaries are reviewed on a regular basis and are benchmarked against similar positions among the peer group companies. Individual salaries are capped at $1 million.

Annual Incentive Compensation. PepsiCo provides performance-related annual incentive compensation to its executive officers under the shareholder-approved 2004 Executive Incentive Compensation Plan ("2004 EIC Plan"). Awards under the 2004 EIC Plan are intended to constitute "performance-based compensation" under Internal Revenue Code Section 162(m). Provided pre-approved targets are achieved, the Committee may exercise negative discretion to determine the exact amount of the incentive to be paid to each executive officer. In exercising this discretion, the Committee considers a broad range of Company and individual performance indicators including PepsiCo's financial results, strategic position and how well the executive manages and develops people. For 2005, the amount of the award an executive was eligible to receive was dependent upon PepsiCo achieving pre-approved earnings targets which were set to achieve third quartile performance relative to peer companies. A payment would not be made if the minimum earnings target was not met.

Long-Term Incentive Compensation. Consistent with PepsiCo's compensation philosophy, the Committee believes that stock ownership and stock-based incentive awards are the best way to align the interests of the executive officers with those of PepsiCo's shareholders. PepsiCo has a long history of linking pay to its long-term stock performance for all employees, not just executives. This is best demonstrated by the fact that, since 1989, PepsiCo has provided an annual grant of stock options to virtually all full-time U.S. employees under its broad-based stock option program, SharePower.

Executives' long-term incentives are comprised of stock options, restricted stock units and a cash incentive which vests over three years. Target grant guidelines for executive officers are developed based on competitive benchmarking. The actual size of grants awarded to executive officers is based primarily on PepsiCo's financial performance relative to peer companies, as well as each officer's individual performance, retention considerations and other special circumstances. The Committee requires that awards made under the long-term incentive plans include vesting terms that encourage an executive officer to remain with PepsiCo over a period of years. All stock option grants have an exercise price equal to the fair market value of PepsiCo Common Stock on the date of grant. There has been no repricing of awards and, under the approved 2003 Long-Term Incentive Plan, any repricing of awards would require shareholder approval.

Historically, following competitive market practice, PepsiCo had utilized stock options as the primary form of long-term incentive compensation. At the end of 2003, the Company voluntarily adopted stock option expensing. Beginning in 2004, consistent with changing market practices that were validated by independent external advisors, the Company reduced the amount of long-term incentives provided to all executives. Concurrent with this change, all executives, except the CEO, were provided with increased performance-based cash incentives. The amount of cash incentives is determined based on achievement of annual performance goals, with payout provided equally over a three year period. Most executives were provided with a choice between stock options and restricted stock units that vest after three years of service. However, PepsiCo's most senior executives, including the CEO, were not provided with this choice. The value of their long-term incentive compensation was fixed equally between stock options and performance-based restricted stock units. In addition, these senior executives do not receive regular awards of service based restricted stock units; they receive performance-based restricted stock units. For these executives to realize the awarded value from the performance-based restricted stock units, the Company must achieve performance targets each year over the following 3-year period. The performance targets during this 3-year period are approved each year by the Board of Directors and are generally set to achieve third quartile financial performance relative to peer companies. Notwithstanding the attainment of the targets, the Board has the discretion to reduce, but not increase, some or all of an award that would otherwise be paid. Executives are not eligible to receive additional shares of restricted stock units above the awarded amount, even when performance targets are exceeded.

Benefits. Executives generally receive the same healthcare and retirement benefits as other employees. Medical benefits are the same for all participants in the Company's health care program; however, executives are required to pay twice as much for their coverage. Because of IRS compensation and benefit limits applicable to the Company's qualified pension plans, a significant portion of executive pensions is typically provided by a non-qualified, unfunded pension plan that provides benefits based on the base salary and annual incentive compensation. Awards of stock options, restricted stock units and the cash incentive that vests over three years are not considered in determining pension benefits. Executive deferrals into the 401(k) Plan, and Company matching contributions are also limited by IRS regulations. While the Company does permit most executives to defer their base salary and annual incentive compensation, PepsiCo does not provide an excess plan to offset 401(k) limitations nor does it provide executives with special benefit plans such as executive life insurance or a pension with an enhanced formula.

CEO Compensation

Mr. Reinemund has held the position of Chairman and Chief Executive Officer since May 2001. The Committee recommends and the Board approves Mr. Reinemund's compensation following the general policies and guidelines described above for the compensation of executive officers. The Committee uses competitive information from peer consumer product companies to establish Mr. Reinemund's above median or "third quartile" target total compensation package and then uses performance against Board approved objectives to determine his actual total compensation.

To establish Mr. Reinemund's target total compensation, the Committee compares his salary, bonus and long-term awards to those of peer Company CEOs. PepsiCo's financial performance is also compared to the peer companies on each of the following measures: net revenue, operating income,

return on capital, EPS and total shareholder return. For 2005 these comparisons were performed by an independent advisor who validated to the Committee that the CEO's target compensation was appropriate given PepsiCo's third quartile financial performance.

To determine Mr. Reinemund's actual total compensation, and whether it should be above or below target, the Committee assesses his performance against target objectives approved by the Board in the beginning of the year. For 2005, financial targets included net revenue, EPS, return on invested capital, and cash flow along with a subjective assessment of how Mr. Reinemund performed against other strategic goals established with the Board.

For the fiscal year 2005, Mr. Reinemund's base salary continued to be capped at $1,000,000. He was eligible for a 2005 annual incentive award because PepsiCo achieved its pre-approved earnings target which was set to achieve third quartile performance relative to peer companies. The Committee then exercised its discretion to determine the amount of the award based on Mr. Reinemund's performance against his target objectives during the year. His 2005 incentive award is shown in the bonus column in the Summary Compensation table that follows.

In February 2005, Mr. Reinemund also received a long-term incentive award which was based on 2004 performance. Part of the award was in stock options, which had an exercise price equal to the fair market value of PepsiCo stock on the day of grant and which vest after three years of service. Part of the award was in performance-based restricted stock units which require that the Company achieve earnings targets over the following three year period before the restrictions can be lifted and value received by Mr. Reinemund. The performance targets during this 3-year period are approved each year by the Board of Directors and are generally set to achieve third quartile financial performance relative to peer companies. Payouts occur at the end of the three year period and no payout for any one of the three years would be made unless the minimum target for that year had been met. Mr. Reinemund is not eligible to receive additional shares of restricted stock units above the awarded amount, even when performance targets are exceeded. Notwithstanding the attainment of the targets, the Board has the discretion to reduce, but not increase, some or all of an award that would otherwise be paid. The stock option and performance-based restricted stock unit awards are shown in the Long-term Compensation columns of the Summary Compensation Table that follows.

Summary

The Committee believes that PepsiCo's compensation practices and compensation philosophy align executive interests with those of shareholders. As the scope and level of an executive's business responsibilities expand, the portion of their compensation package that is "at risk" also increases.

We believe that the actions taken over the past year are appropriate given PepsiCo's performance relative to peer companies and that they will continue to assist the Company to attract, retain and motivate the key talent PepsiCo needs to continue to compete and provide strong returns to shareholders. Effective May 3, 2006, Arthur C. Martinez will become a member of the Compensation Committee.

THE COMPENSATION COMMITTEE

JOHN F. AKERS, CHAIR
ROBERT E. ALLEN
VICTOR J. DZAU

RAY L. HUNT
SHARON PERCY ROCKEFELLER
DANIEL VASELLA

SUMMARY COMPENSATION TABLE

		Annual Compensation			Long-Term Compensation			
					Awards(1)		Payouts	
Name and Principal Position	Year	Salary ($)(2)	Bonus ($)(3)	Other Annual Compensation ($)(4)	Restricted Stock Award(s) ($)(5)	Securities Underlying Options (#)	Long-Term Incentive Plan Payouts ($)	All Other Compensation ($)(6)
Steven S Reinemund	2005	1,000,000	4,500,000	124,614(7)	4,928,553(13)	367,893	0(18)	7,000
Director; Chairman of the Board	2004	1,000,000	4,500,000	170,730(7)	4,157,150	353,198	0	5,154
and Chief Executive Officer	2003	1,000,000	3,800,000	149,393(7)	0	864,717	809,325(19)	0
Michael D. White	2005	837,067	2,121,733	77,098(8)	1,033,505(14)	77,777	198,997(18)	5,212
Director; Vice Chairman –	2004	767,308	1,989,947	129,979(8)	6,033,121	88,444	0	1,784
PepsiCo, Chairman and	2003	721,154	1,449,590	1,462,024(8)	0	235,966	0	0
Chief Executive Officer –								
PepsiCo International								
Indra K. Nooyi	2005	837,067	2,093,373	53,337(9)	1,033,505(15)	77,777	184,503(18)	5,212
Director; President and	2004	767,308	1,845,023	94,221(9)	6,033,121	88,444	0	0
Chief Financial Officer	2003	721,154	1,486,620	125,790(9)	0	235,379	0	0
Irene B. Rosenfeld	2005	813,269	1,414,323	620,745(11)	689,021(16)	51,693	43,056(18)	4,200
Chairman and Chief	2004(10)	247,404	430,556	49,668(11)	1,289,400	23,150	0	4,100
Executive Officer,	2003(10)	0	0	0(11)	0	0	0	0
Frito-Lay N.A.								
John C. Compton	2005	690,923	1,285,290	449,502(12)	633,766(17)	47,799	71,747(18)	7,000
President and Chief	2004	563,077	594,474	43,195(12)	494,991	42,629	0	4,267
Executive Officer,	2003	515,262	473,650	27,286(12)	0	108,590	256,410(19)	0
Quaker-Tropicana-Gatorade								

(1) Long-Term Awards are made at the beginning of the year based on performance during the prior year (e.g., the 2005 Long Term Restricted Stock Units and Option Awards reflect 2004 performance).

(2) Salary amounts reflect actual payments. In 2005, amounts shown reflect the impact of an additional 53rd week, and therefore an additional week of payroll, with the exception of Mr. Reinemund whose base salary is capped at $1 million. Without the 53rd week payment, 2005 figures would have been: $821,115 for Mr. White, $821,115 for Ms. Nooyi, $797,846 for Ms. Rosenfeld, and $677,269 for Mr. Compton.

(3) Bonuses are paid after the end of the year based on performance for that year (e.g., 2005 bonus reflects 2005 performance and is paid in 2006).

(4) Amounts include any personal use of corporate aircraft and ground transportation, car allowance, relocation benefits, and executive physical benefits. Personal use of corporate aircraft and ground transportation is calculated on the basis of aggregate incremental cost to the Company.

(5) Restricted stock units have no value to the recipient until the restrictions are released. The restrictions on any performance-based restricted stock units will be released only upon the achievement of performance targets over a predetermined performance period. Restrictions on any service-based restricted stock units will be released at a future date provided that the recipient remains continuously employed by the Company through that date. During the restriction period, restricted stock units accrue dividend equivalents at the same rate as dividends paid to shareholders. These dividend equivalents will be paid only if the underlying restricted stock units are earned.

(6) Amounts represent the Company matching contributions to the PepsiCo Salaried Employee 401(k) Plan. Executive deferrals into the 401(k) Plan and Company matching contributions are limited by IRS regulations. PepsiCo does not provide an excess plan to offset 401(k) limitations.

(7) For Mr. Reinemund, the personal use of corporate aircraft was $94,835 in 2005, $144,813 in 2004, and $117,479 in 2003, and the personal use of corporate ground transportation was $2,689 in 2005, $1,780 in 2004, and $7,777 in 2003. Mr. Reinemund's car allowance was $24,137 in 2005, $24,137 in 2004 and $24,137 in 2003.

(8) For Mr. White, the personal use of corporate aircraft was $50,383 in 2005, $34,724 in 2004 and $11,930 in 2003, and the personal use of corporate ground transportation was $1,201 in 2005, $0 in 2004, and $0 in 2003. Mr. White's car allowance was $24,137 in 2005, $24,137 in 2004 and $13,925 in 2003. Mr. White relocated from Switzerland to New York in 2003 after assuming his role as Chairman and CEO of PepsiCo International. Amounts also include incremental taxes of $70,086 in 2004 and $1,173,313 in 2003 that were required to be paid primarily to Switzerland as a result of Mr. White's multi-year assignment outside of the United States. 2003 amounts also include $167,954 paid in connection with Mr. White's repatriation from Switzerland.

(9) For Ms. Nooyi, the personal use of corporate aircraft was $20,800 in 2005, $57,104 in 2004, and $95,810 in 2003, and the personal use of corporate ground transportation was $7,024 in 2005, $11,780 in 2004, and $7,042 in 2003. Ms. Nooyi's car allowance was $24,137 in 2005, $25,336 in 2004 and $22,937 in 2003.

(10) Ms. Rosenfeld joined PepsiCo, Inc. as Chairman and CEO of the Company's Frito-Lay North America division on September 1, 2004.

(11) Ms. Rosenfeld relocated from Chicago to Dallas after assuming her role as Chairman and CEO of Frito-Lay. Amounts include relocation expenses and applicable reimbursement of taxes of $475,503 in 2005 and $11,752 in 2004 delivered under the relocation program available to all PepsiCo employees. For Ms. Rosenfeld, the personal use of corporate aircraft was $121,573 in 2005, of which $62,484 related to travel between Chicago and Dallas, and $30,360 in 2004. The personal use of corporate ground transportation was $0 in 2005 and $0 in 2004. Ms. Rosenfeld's car allowance was $23,669 in 2005 and $7,556 in 2004.

(12) Mr. Compton relocated from Dallas to Chicago in 2005 after assuming his role as President and CEO of Quaker-Tropicana-Gatorade. The 2005 amount includes relocation expenses and applicable reimbursement of taxes of $386,052 delivered under the relocation policy offered to all PepsiCo employees. For Mr. Compton, the personal use of corporate aircraft was $40,098 in 2005, $20,848 in 2004, and $6,065 in 2003, and the personal use of corporate ground transportation was $0 in 2005, $0 in 2004, and $0 in 2003. Mr. Compton's car allowance was $23,352 in 2005, $21,222 in 2004 and $21,222 in 2003.

(13) On February 1, 2005, Mr. Reinemund received a grant of 91,694 performance-based restricted stock units having a value of $4,928,553 on that date. Restrictions on this grant will only be released upon the achievement of performance targets over the 3-year performance period (2005-2007). Including the February 1, 2005 grant, the aggregate value of Mr. Reinemund's total 179,676 restricted stock units as of December 31, 2005 was $10,615,258 (Based on the closing price of PepsiCo Common Stock on December 30, 2005).

(14) On February 1, 2005, Mr. White received a grant of 19,228 performance-based restricted stock units having a value of $1,033,505 on that date. Restrictions on this grant will only be released upon the achievement of performance targets over the 3-year performance period (2005-2007). Including the February 1, 2005 grant, the aggregate value of Mr. White's total 146,913 restricted stock units as of December 31, 2005 was $8,679,620 (Based on the closing price of PepsiCo Common Stock on December 30, 2005).

(15) On February 1, 2005, Ms. Nooyi received a grant of 19,228 performance-based restricted stock units having a value of $1,033,505 on that date. Restrictions on this grant will only be released upon the achievement of performance targets over the 3-year performance period (2005-2007). Including the February 1, 2005 grant, the aggregate value of Ms. Nooyi's total 146,913 restricted stock units as of December 31, 2005 was $8,679,620 (Based on the closing price of PepsiCo Common Stock on December 30, 2005).

(16) On February 1, 2005, Ms. Rosenfeld received a grant of 12,819 performance-based restricted stock units having a value of $689,021 on that date. Restrictions on this grant will only be released upon the achievement of performance targets over the 3-year performance period (2005-2007). Including the February 1, 2005 grant, the aggregate value of Ms. Rosenfeld's total 18,607 restricted stock units as of December 31, 2005 was $1,099,302 (Based on the closing price of PepsiCo Common Stock on December 30, 2005).

(17) On February 1, 2005, Mr. Compton received a grant of 11,791 performance-based restricted stock units having a value of $633,766 on that date. Restrictions on this grant will only be released upon the achievement of performance targets over the 3-year performance period (2005-2007). Including the February 1, 2005 grant, the aggregate value of Mr. Compton's total 22,267 restricted stock units as of December 31, 2005 was $1,315,534 (Based on the closing price of PepsiCo Common Stock on December 30, 2005).

(18) All executives, with the exception of the CEO, are eligible for a long-term cash incentive, which is determined based on the achievement of annual performance goals. To facilitate retention, payment of this incentive is provided equally over three years, contingent upon continued employment through December 31 of each year. The 2005 long-term payouts reflect one-third of the 2004 performance-based, long-term cash incentive earned with 2005 service.

(19) These amounts were awarded under a long-term incentive program which was eliminated in 2000 with final payments made in 2003. 2003 payments were based on performance during the prior three year period 2000-2002.

OPTION GRANTS IN LAST FISCAL YEAR

	Individual Grants				Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term	
Name	Number of Securities Underlying Options Granted(#)	% of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price ($/Sh)	Expiration Date	5% ($)(2)	10% ($)(2)
Steven S Reinemund	367,893(1)	2.98%	$53.75	1/31/2015	$12,435,919	$31,515,060
Michael D. White	77,777(1)	0.63%	$53.75	1/31/2015	$ 2,629,103	$ 6,662,662
Indra K. Nooyi	77,777(1)	0.63%	$53.75	1/31/2015	$ 2,629,103	$ 6,662,662
Irene B. Rosenfeld	51,693(1)	0.42%	$53.75	1/31/2015	$ 1,747,383	$ 4,428,211
John C. Compton	47,799(1)	0.39%	$53.75	1/31/2015	$ 1,615,754	$ 4,094,637

(1) These options become exercisable on February 1, 2008.

(2) The 5% and 10% rates of appreciation were set by the SEC and are not intended to forecast future appreciation, if any, of PepsiCo's stock. If PepsiCo's stock does not increase in value, then the option grants described in the table will be valueless.

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FY-END OPTION VALUES (1)

Name	Shares Acquired on Exercise(#)	Value Realized	Number of Securities Underlying Unexercised Options at Fiscal Year-End		Value of Unexercised In the Money Options at Fiscal Year-End	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Steven S Reinemund	319,784	$7,700,456	2,912,544	3,085,808	$63,935,747	$43,209,182
Michael D. White	116,861	$3,201,711	767,982	653,479	$14,931,432	$ 9,754,541
Indra K. Nooyi	114,847	$2,223,064	703,962	1,104,771	$12,934,350	$15,283,015
Irene B. Rosenfeld	0	$ 0	0	74,843	$ 0	$ 485,726
John C. Compton	75,206	$1,956,142	577,730	649,018	$11,586,278	$11,069,114

(1) The closing price of PepsiCo Common Stock on December 30, 2005, the last trading day prior to PepsiCo's fiscal year end, was $59.08

EMPLOYMENT ARRANGEMENTS

Irene B. Rosenfeld entered into an employment arrangement with PepsiCo to serve as Chairman and Chief Executive Officer of the Company's Frito Lay North American division commencing September 1, 2004. The employment arrangement does not guarantee employment and either the Company or Ms. Rosenfeld may terminate her employment at any time. The employment arrangement provides for a payout equal to one year of base salary and bonus should she be involuntarily terminated (other than for cause) within the first three years of her employment.

The arrangement provided Ms. Rosenfeld with relocation benefits generally available to all employees to facilitate her relocation from Chicago to Dallas. She was also granted $1 million in Restricted Stock Units with one-year service-based vesting. The award vested on September 1, 2005 and converted to common shares, less applicable taxes. The shares are currently being held by Ms. Rosenfeld in furtherance of her share ownership requirements.

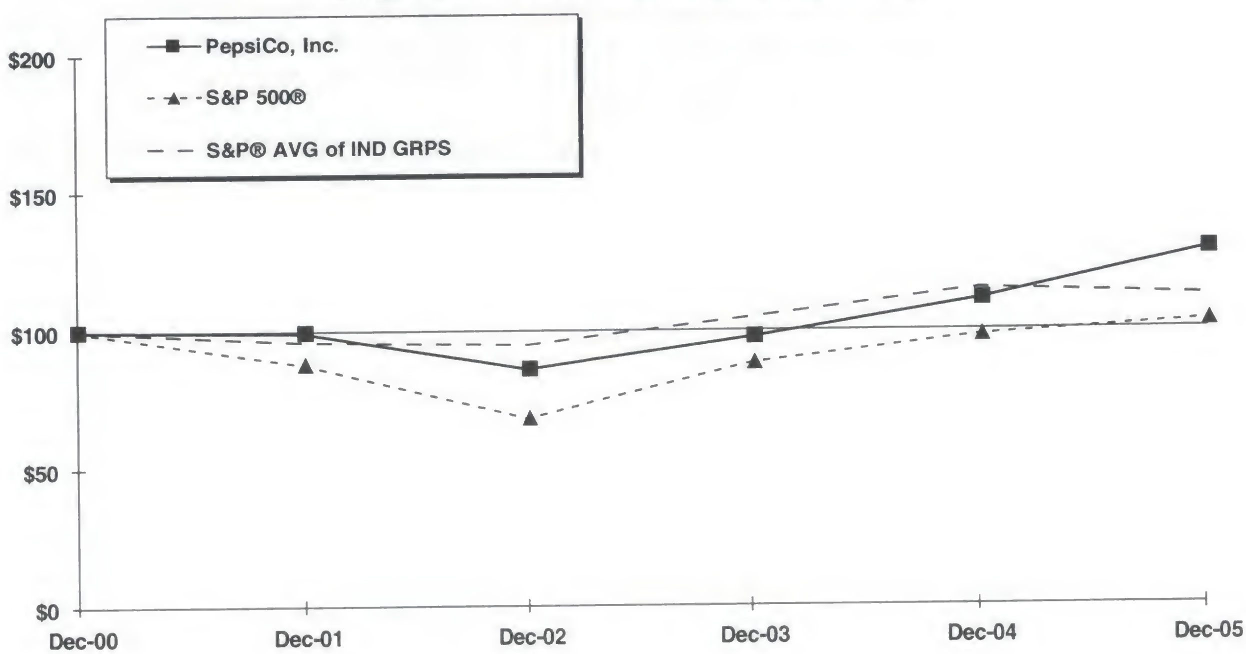
As part of the arrangement, Ms. Rosenfeld is eligible to receive salary, bonus, long-term incentives and other benefits as described in both the "Summary Compensation Table" and "Compensation Committee Report" contained in this Proxy Statement. Her bonus and long-term incentives are awarded based on performance and all elements of her compensation, including salary, are subject to yearly review by the Board of Directors based on the Company's and Ms. Rosenfeld's performance.

Ms. Rosenfeld participates in the same retirement program as other salaried employees and will be eligible for full retirement at age 62 after ten years of service. At that time, as part of the arrangement, she will receive an additional 10 years of credited service when determining her retirement benefit.

PERFORMANCE GRAPH

The line below labeled S&P Average of Industry Groups is derived by weighting the returns of two applicable S&P Industry Groups (Non-Alcoholic Beverages and Food) by PepsiCo's sales in its Beverage and Food businesses. The return on PepsiCo stock investment, the S&P 500 and the S&P Average indices are calculated through the last trading day of PepsiCo's fiscal year end, December 30, 2005.

CUMULATIVE TOTAL RETURN,
using PepsiCo's quarterly revenue weightings



PENSION PLAN TABLE

When an executive retires at the normal retirement age (65), the approximate annual benefits payable after January 1, 2006 for the following pay classifications and years of service are:

Remuneration	Years of Service					
	15	20	25	30	35	40
$1,000,000	346,710	395,610	444,520	493,420	542,320	592,320
$1,250,000	434,210	495,610	557,020	618,420	679,820	742,320
$1,500,000	521,710	595,610	669,520	743,420	817,320	892,320
$1,750,000	609,210	695,610	782,020	868,420	954,820	1,042,320
$2,000,000	696,710	795,610	894,520	993,420	1,092,320	1,192,320
$2,500,000	871,710	995,610	1,119,520	1,243,420	1,367,320	1,492,320
$3,000,000	1,046,710	1,195,610	1,344,520	1,493,420	1,642,320	1,792,320
$3,500,000	1,221,710	1,395,610	1,569,520	1,743,420	1,917,320	2,092,320
$4,000,000	1,396,710	1,595,610	1,794,520	1,993,420	2,192,320	2,392,320
$4,500,000	1,571,710	1,795,610	2,019,520	2,243,420	2,467,320	2,692,320
$5,000,000	1,746,710	1,995,610	2,244,520	2,493,420	2,742,320	2,992,320

The pay covered by the Pension Plans noted below is based on the salary and annual bonus included in the Summary Compensation Table in this Proxy Statement for each of our five most highly compensated executive officers. The years of credited service as of January 1, 2006 for the executive officers named on the Summary Compensation Table are: Steven S Reinemund—21 years; Indra K. Nooyi—11 years; Michael D. White—15 years; Irene B. Rosenfeld—1 year; John C. Compton—22 years.

Computation of Benefits

PepsiCo's executive officers generally participate in PepsiCo's Salaried Employees Retirement Plan and PepsiCo's Pension Equalization Plan (which has been adopted to provide benefits that would have been payable under the Retirement Plan except for ERISA and Internal Revenue Code limitations). The annual benefits payable under these two Pension Plans to employees with 5 or more years of service at age 65 are, for the first 10 years of credited service, 3% of the employee's highest consecutive five-year average annual earnings plus an additional 1% of the employee's highest consecutive five-year average annual earnings for each additional year of credited service over 10 years, less 0.43% of final average earnings not to exceed Social Security covered compensation multiplied by years of service (not to exceed 35 years).

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16 of the Securities Exchange Act of 1934 requires PepsiCo's directors and executive officers to file reports of ownership and changes in ownership of PepsiCo Common and Convertible Preferred Stock. We received written representations from each such person who did not file an annual report with the SEC on Form 5 that no Form 5 was due. To the best of PepsiCo's knowledge, in 2005, all required forms were filed on time with the Securities and Exchange Commission.

RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANTS (PROXY ITEM NO. 2)

The Audit Committee engaged KPMG LLP ("KPMG") as PepsiCo's independent registered public accountants for 2006, subject to ratification by shareholders. KPMG has served as PepsiCo's independent auditors since 1990.

Representatives of KPMG will be available to answer appropriate questions at the Annual Meeting and are free to make statements during the meeting.

The Board of Directors recommends that shareholders vote FOR the ratification of the appointment of KPMG as PepsiCo's independent registered public accountants for 2006.

SHAREHOLDER PROPOSALS

If proposals are submitted by more than one shareholder, PepsiCo will only list the primary filer's name, address and number of shares held. We will provide information about co-filers promptly if we receive a request for the information.

POLITICAL CONTRIBUTIONS (PROXY ITEM NO. 3)

Mrs. Evelyn Y. Davis, Watergate Office Building, 2600 Virginia Avenue, N.W., Washington, D.C. 20037, who owns 900 shares of PepsiCo Common Stock, has submitted the following resolution for the reasons stated:

"RESOLVED: That the stockholders recommend that the Board direct management that within five days after approval by the shareholders of this proposal, the management shall publish in newspapers of general circulation in the cities of New York, Washington, D.C., Detroit, Chicago, San Francisco, Los Angeles, Dallas, Houston and Miami, and in the Wall Street Journal and USA Today, a detailed statement of each contribution made by the Company, either directly or indirectly, within the immediately preceding fiscal year, in respect of a political campaign, political party, referendum or citizens' initiative, or attempts to influence legislation, specifying the date and amount of each such contribution, and the person or organization to whom the contribution was made. Subsequent to this initial disclosure, the management shall cause like data to be included in each succeeding report to shareholders. And if no such disbursements were made, to have that fact publicized in the same manner.

REASONS: This proposal, if adopted, would require the management to advise the shareholders how many corporate dollars are being spent for political purposes and to specify what political causes the management seeks to promote with those funds. It is therefore no more than a requirement that the shareholders be given a more detailed accounting of these special purpose expenditures that they now receive. These political contributions are made with dollars that belong to the shareholders as a group and they are entitled to know how they are being spent. Last year the owners of 89,404,156 shares, representing approximately 8.1% of shares voting, voted FOR this proposal.

If you AGREE, please mark your proxy FOR this resolution."

Response: PepsiCo believes that it is essential that we, both as a Company and as individuals, be responsibly engaged in the public policy and political arenas. We also believe that shareholders should be provided with information on how their company is spending resources for political purposes. PepsiCo has always disclosed this information as required by law and regulations. In 2005, PepsiCo developed a Political Contributions Policy that provides shareholders with details on the policies, procedures and criteria used in connection with all political contributions. The Political Contributions Policy is posted on our website www.*pepsico.com* in the "Investors" section under "Corporate Governance – Policies." In addition, details on PepsiCo's political contributions will be posted on our website on an annual basis, beginning with the release of PepsiCo's Corporate Citizenship Report in 2006. Shareholders were included in the discussions leading to the development of the Policy.

The Proponent's resolution calls for publishing this information in newspapers of selected local and national newspapers. PepsiCo believes that publishing this information on our website is more efficient and cost effective.

The Board of Directors recommends that shareholders vote AGAINST this resolution.

CHARITABLE CONTRIBUTIONS (PROXY ITEM NO. 4)

The National Legal and Policy Center, 107 Park Washington Court, Falls Church, Virginia 22046, who owns 54 shares of PepsiCo Common Stock, has submitted the following resolution for the reasons stated:

"Whereas: Company executives exercise wide discretion over the use of corporate assets for charitable purposes. Absent a system of accountability for charitable contributions, Company executives may use Company's assets for objectives that are not shared by and may be inimical to the interests of the Company and its shareholders, potentially harming long-term shareholder value. See National Legal and Policy Center, *http://www.nlpc.org/cip.asp* and Free Enterprise Action Fund, *http://www.FreeEnterpriseActionFund.com.*

Principles of transparency and accountability should apply to Company charitable contributions. Such disclosure is consistent with public policy in regard to disclosure by publicly-owned companies.

Whereas: According to the 2004 PepsiCo Annual Report, "We give to nonprofit community groups and initiatives through the PepsiCo Foundation, PepsiCo Community Affairs and our various operating divisions. Additionally, we provide gifts-in-kind, support community and nonprofit events, conventions and journals and sponsor meetings." According to the same Annual Report, such gifts totaled $71.9 million in 2004.

Whereas: Shareholders are entitled to know how their company is spending its funds for charitable purposes.

RESOLVED: That the shareholders request that the Company provide a report updated semi-annually, omitting proprietary information and at reasonable cost, disclosing the Company's:

1. Policies and procedures for charitable contributions (both direct and indirect) made with corporate assets;

2. Monetary and non-monetary contributions made to non-profit organizations operating under Section 501(c)(3) and 501(c)(4) of the Internal Revenue Code, and any other public or private charitable organizations;

3. Business rationale for each of the charitable contributions;

4. Personnel who participated in making the decisions to contribute; and

5. To the extent reasonably possible, the actual or estimated benefits to the Company and beneficiaries produced by contributions.

To the extent reasonable and permissible, the report may include the type of information requested above for charities controlled or managed by the Company, including The PepsiCo Foundation. This report may be posted on the Company's website to reduce costs to shareholders.

REASONS: Current disclosure is insufficient to allow the Company's Board and its shareholders to fully evaluate the charitable use of corporate assets.

There is currently no single source providing shareholders the information sought by this resolution. Details of contributions only sometimes become known when publicized by recipients. Two Company contributions to the Rainbow/PUSH coalition were disclosed in Rainbow/PUSH conference programs in 2005.

If you AGREE, please mark your proxy FOR this resolution."

Response: PepsiCo believes that shareholders should be provided with information on how their company is spending funds for charitable purposes. PepsiCo has been providing this information since 1999.

PepsiCo provides information on the PepsiCo Foundation, charitable donations and activities involving nonprofit organizations, including information on amounts donated, policies and procedures, charitable organizations supported and the primary platforms to be achieved with corporate contributions. These areas are currently health and wellness, diversity, education, and employees, as well as donations relating to disaster relief.

In 2005, the PepsiCo Foundation began work to enrich the PepsiCo website with more detail on charitable contributions. Discussions with shareholder groups including the Proponent, National Legal and Policy Center, contributed to further developing the information. The PepsiCo website now includes detailed disclosure regarding 2005 contributions made by the PepsiCo Foundation, PepsiCo and PepsiCo divisions. This information can be found on our website www.*pepsico.com* in the "Citizenship" section under "Contributions." The website also includes information on governance and procedures, and the specific focus area to identify the rationale for each contribution. The information on the website will be updated with significant new grants on an ongoing basis throughout the year.

The Company believes that the enhanced disclosure already provided on the website is the most efficient and effective use of the Company's resources.

The Board of Directors recommends that shareholders vote AGAINST this resolution.

OTHER MATTERS

The Board of Directors knows of no other matters to be brought before the Annual Meeting.

2007 SHAREHOLDERS' PROPOSALS

PepsiCo welcomes comments or suggestions from its shareholders. If a shareholder wants to have a proposal formally considered at the 2007 Annual Meeting of Shareholders, and included in the Proxy Statement for that Meeting, we must receive the proposal in writing on or before November 24, 2006. In addition, if a shareholder proposal is not received by us on or before February 2, 2007, under PepsiCo's By-Laws it will not be considered or voted on at the Annual Meeting.

GENERAL

PepsiCo will pay the costs relating to this Proxy Statement, the proxy and the Annual Meeting.

In addition to the solicitation of proxies by mail and electronically, PepsiCo intends to ask brokers and bank nominees to solicit proxies from their principals and will pay the brokers and bank nominees their expenses for the solicitation. Employees of PepsiCo may also solicit proxies. They will not receive any additional pay for the solicitation.

To be sure that we have the necessary quorum to hold the Annual Meeting, PepsiCo has hired the firm of Georgeson Shareholder Communications Inc. to help in soliciting proxies by mail, telephone and personal interview for fees estimated at approximately $21,000.

The Annual Report to Shareholders for 2005, including financial statements, was delivered with this Proxy Statement or was previously delivered to shareholders and is not part of the material for the solicitation of proxies. To reduce postage costs, we sent materials at bulk mail rates. If you have not received the Annual Report by the time you receive your Proxy Statement, please contact PepsiCo's Manager of Shareholder Relations, at PepsiCo, Inc., 700 Anderson Hill Road, Purchase, NY 10577 or (914) 253-3055.

Shareholders can help us reduce the cost of printing and mailing the Proxy Statement and the Annual Report by opting to receive future materials electronically. To enroll, please visit our website at *www.pepsico.com,* click on the "Investors — Shareholder Information — Electronic Delivery Enrollment" links and follow the instructions provided.

A copy of PepsiCo's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (without exhibits) will be sent to any shareholder without charge by contacting the Company at the address or phone number listed above. You also may obtain our Annual Report on Form 10-K over the Internet at the Securities and Exchange Commission's website, www.sec.gov, or at our website, *www.pepsico.com.*

Please vote your shares promptly through any of the means described on the proxy card.

By order of the Board of Directors,

Larry D. Thompson
Secretary

Exhibit A

PepsiCo, Inc.

CORPORATE GOVERNANCE GUIDELINES

As of February 3, 2006

The Board of Directors (the "Board") of PepsiCo, Inc. (the "Corporation"), acting on the recommendation of its Nominating and Corporate Governance Committee, has developed and adopted certain corporate governance principles (the "Guidelines") establishing a common set of expectations to assist the Board and its committees in performing their duties in compliance with applicable requirements. In recognition of the continuing discussions about corporate governance, the Board will review and, if appropriate, revise these Guidelines from time to time.

A. *Director Responsibilities*

1. Represent the interests of the Corporation's shareholders in maintaining and enhancing the success of the Corporation's business, including optimizing long-term returns to increase shareholder value.
2. Selection and evaluation of a well-qualified Chief Executive Officer ("CEO") of high integrity, and approval of other members of the senior management team.
3. Oversee and interact with senior management with respect to key aspects of the business including strategic planning, management development and succession, operating performance, and shareholder returns.
4. Provide general advice and counsel to the Corporation's CEO and senior executives.
5. Adopt and oversee compliance with the Corporation's Worldwide Code of Conduct. Promptly disclose any waivers of the Code of Conduct for Directors or executive officers.
6. Hold regularly scheduled executive sessions of independent directors. Designate and publicly disclose the name of the Director who will preside at such meetings. Formally evaluate the performance of the CEO and senior management each year in executive sessions.
7. Regular attendance at Board meetings is mandatory. Meeting materials should be reviewed in advance.
8. *Duty of Care:* In discharging the duties of a Director, including duties as a Committee member, North Carolina law requires that a Director shall act: (1) in good faith; (2) with care an ordinary prudent person in a like position would exercise under similar circumstances and (3) in a manner he or she believes to be in the best interests of the Corporation.

B. *Director Qualification Standards*

1. The Nominating and Corporate Governance Committee, with the input of the CEO, is responsible for recommending to the Board (1) nominees for Board membership to fill vacancies or newly created positions and (2) the persons to be nominated by the Board for election at the Corporation's Annual Meeting of Shareholders. The Nominating and Corporate Governance Committee does not solicit Director nominations, but will consider recommendations sent to the Secretary of the Corporation at 700 Anderson Hill Road, Purchase, New York 10577.
2. In connection with the selection and nomination process, the Nominating and Corporate Governance Committee shall review the desired experience, mix of skills and other qualities to assure appropriate Board composition, taking into account the current Board members and the specific needs of the Corporation and the Board. The Board will generally look for individuals who have displayed high ethical standards,

integrity, and sound business judgment. This process is designed to ensure that the Board includes members with diverse backgrounds, skills and experience, including appropriate financial and other expertise relevant to the business of the Corporation.

3. Independent directors must comprise a majority of the Board.

4. An independent director of the Corporation is a director who:

   (a) is not and has not been an employee, and does not have an immediate family member[1] who is or has been an executive officer[2], of the Corporation, or any of its consolidated subsidiaries, during the last three years;

   (b) has not received, and does not have an immediate family member who has received, more than $100,000 in direct compensation from the Corporation, or any of its consolidated subsidiaries, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service) during any twelve month period within the last three years;

   (c) (i) is not, and does not have an immediate family member that is, a current partner of a firm that is the Corporation's, or any of its consolidated subsidiaries', internal or external auditor; (ii) is not a current employee of such external audit firm; (iii) does not have an immediate family member who is a current employee of such external audit firm who participates in such firm's audit, assurance or tax compliance (but not tax planning) practice; and (iv) was not, and does not have an immediate family member that was, within the last three years (but is no longer) a partner or employee of such external audit firm who personally worked on the Corporation's, or any of its consolidated subsidiaries', audit within that time;

   (d) is not and has not been, and does not have an immediate family member who is or has been, within the last three years, employed as an executive officer of another company where any of the Corporation's, or any of its consolidated subsidiaries', present executive officers at the same time serves or served on such other company's compensation committee;

   (e) is not a current employee of, and does not have an immediate family member who is a current executive officer of, another company that has made payments to, or has received payments from, the Corporation, or any of its consolidated subsidiaries, for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of $1 million or 2% of the consolidated gross revenues of such other company for its last completed fiscal year; and

   (f) has no other material relationship with the Corporation, or any of its consolidated subsidiaries, either directly or as a partner, shareholder or officer of an organization that has a material relationship with the Corporation, or any of its consolidated subsidiaries.

   In making a determination regarding a proposed director's independence, the Board shall consider all relevant facts and circumstances, including the director's commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships, and such other criteria as the Board may determine from time to time. If a proposed director serves as an executive officer, director or trustee of a tax exempt organization, such relationship will not be considered to be a material relationship that would impair

[1] An "immediate family member" is defined to include a person's spouse, parents, children, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law and anyone (other than domestic employees) who shares such person's home. In considering a director's independence, the Corporation need not consider individuals who are no longer immediate family members as a result of legal separation or divorce, or those who have died or become incapacitated.

[2] An "executive officer" means one of the Section 16 officers designated by a company.

a director's independence if contributions from the Corporation, or any of its consolidated subsidiaries, to such tax exempt organization in any of the last three fiscal years are less than the greater of (i) $1 million or (ii) 2% of the consolidated gross revenues of such tax exempt organization for its last completed fiscal year.

5. In addition to satisfying all of the independence criteria set forth in paragraph 4 of this Section, all members of the Audit Committee must also meet the following requirements:

   (a) Director's fees are the only compensation that members of the Audit Committee may receive from the Corporation or any of its consolidated subsidiaries. Audit Committee members may not receive consulting, advisory or other compensatory fees from the Corporation or any of its consolidated subsidiaries (other than in his or her capacity as a member of the Audit Committee, the Board of Directors, or any other committee of the Board).

   (b) No member of the Audit Committee may be an "affiliated person" of the Corporation, or any of its consolidated subsidiaries, as such term is defined by the Securities and Exchange Commission.

6. Directors must retire at the age of 72, effective upon the expiration of their annual term at the next Annual Meeting of Shareholders.

7. The number of boards on which a Director may sit may be reviewed on a case-by-case basis by the Nominating and Corporate Governance Committee. Prior to accepting any position on the Board of Directors of any non-profit or for-profit organization, the Director shall notify the office of Corporate Secretary. The number of audit committees on which the Corporation's audit committee members may sit concurrently shall be reviewed annually by the Nominating and Corporate Governance Committee and the Board.

8. The Board has not established term limits for Directors. Although term limits can promote the inclusion on the Board of people with diverse perspectives, the process described in paragraph 2 of this Section can achieve the same result. Moreover, term limits have the disadvantage of causing the Corporation to lose the contributions of Directors who have been able to develop over a period of time, increasing insight into the Corporation and its operations, thereby increasing their contributions to the Corporation.

9. A Director shall offer, in writing, to resign if there is any significant change in his or her personal circumstances, including a fundamental change in his or her job responsibilities. The Chairman of the Nominating and Corporate Governance Committee may recommend, to the full Board, acceptance or rejection of such an offer after consultation with the Committee members and the Chairman of the Board.

C. Board Committees

1. The Board shall at all times have a Nominating and Corporate Governance Committee, an Audit Committee and a Compensation Committee, each comprised solely of independent directors.

2. The Board shall evaluate and determine the circumstances under which to form new Committees.

3. The Nominating and Corporate Governance Committee shall annually review succession plans for the members of the Board, the members of the Committees of the Board, and the Chair of the Committees of the Board.

D. Director Compensation

1. Non-employee directors and committee chairs shall receive reasonable compensation for their services, as may be determined from time to time by the Board upon recommendation of the Nominating and Corporate Governance Committee.

Compensation for non-employee directors and committee chairs shall be consistent with the market practices of other similarly situated companies but shall not be at a level or in a form that would call into question the Board's objectivity. The Nominating and Corporate Governance Committee of the Board shall annually review and report to the Board with respect to director compensation and benefits.

2. Directors who are employees receive no additional pay for serving as Directors.

3. Directors who are members of the Audit Committee may receive no compensation from the Corporation other than the fees they receive for serving as Directors.

E. Director Access to Management and Independent Advisors

1. The Board is expected to be highly interactive with senior management. Directors are granted access to the name, location, and phone number of all employees of the Corporation.

2. It is Board policy that executive officers and other members of senior management who report directly to the CEO be present at Board meetings at the invitation of the Board. The Board encourages such executive officers and senior management to make presentations, or to include in discussions at Board meetings managers and other employees who (1) can provide insight into the matters being discussed because of their functional expertise and/or personal involvement in such matters and/or (2) are individuals with high potential whom such executive officers and senior management believe the Directors should have the opportunity to meet and evaluate.

3. Directors are authorized to consult with independent advisors, as is necessary and appropriate, without consulting management.

F. Director Orientation and Continuing Education

1. The Board shall implement and maintain an orientation program for newly elected directors.

2. Directors are required to continue educating themselves with respect to international markets, accounting and finance, leadership, crisis response, industry practices, general management, and strategic planning.

G. Management Succession and CEO Compensation

1. The CEO shall provide an annual report to the Board assessing senior managers and their potential to succeed him or her, and such report shall be developed in consultation with the Chairman of the Compensation Committee and include plans in the event of an emergency or retirement of the CEO. The report shall also contain the CEO's recommendation as to his or her successor.

2. The Board has the primary responsibility for plans for succession to the position of Chief Executive Officer. The Compensation Committee oversees preparation of succession plan presentations to the Board. The Committee Chairman works with the CEO in preparation of the succession plan presentations. The Committee undertakes such follow-up steps with respect to succession planning as may be delegated by the Board from time to time.

3. The Compensation Committee is responsible for making recommendations to the Board concerning annual and long-term performance goals for the CEO and for evaluating his or her performance against such goals.

H. Annual Performance Evaluation of the Board

1. The Board and its Committees will conduct a self-evaluation at least annually to determine whether it and its Committees are functioning effectively.

2. The Board will also review the Nominating and Corporate Governance Committee's periodic recommendations concerning the performance and effectiveness of the Board and its Committees.

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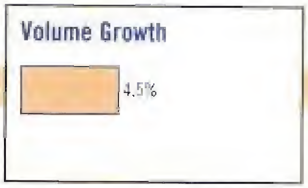
PepsiCo at a Glance

$ in Millions

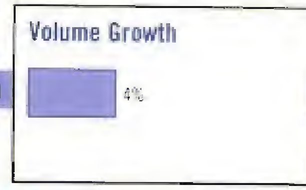
Frito-Lay North America



Net Revenue

Operating Profit

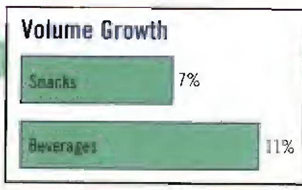
PepsiCo Beverages North America



Net Revenue

Operating Profit

PepsiCo International

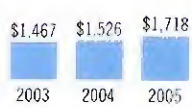


Net Revenue

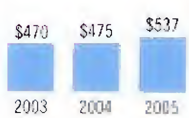
Operating Profit

Quaker Foods North America

Net Revenue



Operating Profit



Dear Shareholders:

With profitable growth across all divisions, on every continent and across both convenient food and beverage categories, PepsiCo delivered a very strong 2005. The company's continued focus on health and wellness, and innovation — coupled with its efforts to build big, muscular brands and powerful go-to-market systems — generated industry leading results.

- **Volume grew 7%.**
- **Net revenue grew 11%.**
- **Division operating profit grew 10%.**
- **Earnings per share grew 15%.***
- **Total return to shareholders was 15% compared with 5% for the S&P.**
- **Cash flow from operations was $5.9 billion and management operating cash flow was $4.2 billion.****

Steve Reinemund
Chairman and Chief Executive Officer

What's particularly pleasing about these results is the balance they represent. Whether it's between foods and beverages, North American and International operations, or even different parts of the day, our portfolio of leading brands finds convenient ways into consumers' lives any time of day, anywhere across the globe.

That's why this year's report focuses on what your company is doing to capture growth opportunities on any given day across the world. It's a departure from previous annual reports which focused primarily on each division's operating performance. While you can still find division summaries in this report, we want to give you a more holistic view of how your company is seeking to capture growth opportunities.

You'll see these opportunities addressed in the key themes in the pages that follow, but we also recognize that there are specific questions to which many investors seek answers. Over the last year, we've collected key questions shareholders most often ask about our businesses; they reflect issues we spend significant time and energy addressing. And first, on just about everyone's list, is what PepsiCo is doing in the area of health and wellness.

2005 Scorecard

* See page 76.
** See page 49.

There is a lot in the press about the "obesity epidemic." How urgent is the obesity issue, and does it pose a risk to PepsiCo's business?

There is no question that obesity is a significant issue gaining increased attention and importance in many nations. Public health is a complex issue that requires partnerships across public and private sectors to find solutions that help consumers.

That's why, while we view this issue as a challenge, we also see the growing interest in health and wellness as a growth opportunity. Given that North America revenues from our Smart Spot eligible products — more than 250 products that contribute to healthier lifestyles — grew at more than two-and-one-half times the rate of the rest of our portfolio in 2005, it's clear that our strategy is aligned with the interests of our consumers and retail partners. And it's the right thing to do for our business. As a result, our commitment to health and wellness has never been stronger.

We believe the solution to consumers' health and wellness needs — and the obesity epidemic in particular — lies in the concept of energy balance; that is, finding balance between the calories consumed and the calories burned. It requires companies like PepsiCo to be part of the solution — a priority on which we will continue to take action.

Whether it's reformulating our products with lower sugar, fat or sodium, adding new or additional ingredients that deliver health benefits, or developing entirely new products, we've committed considerable resources to doing what we do best — giving consumers what they want. We've also committed to supporting active lifestyles and marketing responsibly, and I'd encourage you to read details surrounding all our work in health and wellness later in this report.

Your commitment to the International business seems to be paying off. What are the drivers of growth in your International business, and do you expect the growth to continue at the same pace?

The outstanding growth achieved by our International business in 2005 is the result of years of investment and the implementation of a deliberate strategy to create scale in key international markets that will deliver profitable growth. As the fastest growing division at PepsiCo — and now the largest revenue generator — PepsiCo International's strategy clearly is delivering results.

To give more perspective on why we're encouraged about our international growth prospects, the portfolio of international markets is both broadening and strengthening, as we deliver exciting new products, tailored to local tastes, to consumers in more than 200 countries and territories. We're particularly pleased with our growing presence in key emerging markets such as Brazil, China, India and Russia.

We're very proud of the growth generated through our brands. Our performance is directly attributable to the passionate people who run our businesses in our international markets, each and every day of the year, adapting our products, packaging and distribution systems to a wide variety of tastes and market conditions.

We continue to expect our International business to grow at about twice the rate of our North American businesses, though favorable global macroeconomics clearly contributed to our 2005 performance which exceeded that expectation.

What is the role of acquisitions in PepsiCo's future growth?

We continue to believe that small, strategic, or "tuck in" acquisitions, will help propel our future growth. Our recent acquisitions of Sakata in Australia, Star Foods in Poland, Punica in Germany, P.J. Smoothies in the United Kingdom and Stacy's Pita Chips in the United States, are clear examples of how smaller acquisitions that offer considerable synergies with our existing businesses can help us grow in new geographies and new categories.

In each case, we exercise a disciplined approach to assessing any opportunity, carefully reviewing both strategic and financial criteria to ensure a fit with PepsiCo.

It's important to understand that while acquisitions have a role to play in our growth plans, we believe we'll continue to experience strong "organic" growth in our existing portfolio of businesses. They're equipped with big, muscular brands, they have room to grow, and they receive constant investment and attention.

The carbonated soft drink category in North America has slowed in recent years. What does this trend mean for PepsiCo's growth prospects?

While our carbonated soft drink business was down in North America in 2005, we're convinced that, over time, growth can be restored as we continue to invest in innovation for our carbonated beverages. Our diet carbonated soft drinks continue to grow in North America, an indication that consumers will remain engaged with the category if we offer carbonated soft drinks they desire.

Importantly, if you look at the total liquid refreshment beverage (LRB) category in North America — meaning all beverage occasions except for coffee, alcohol, tap and bulk water — you'll see it's growing at about 2.5% annually. This is consistent with historical growth rates for LRB, and PepsiCo is very well positioned to capture this growth.

That's because we have an advantaged portfolio of non-carbonated beverages, which is exactly where the growth in LRB is, and where we believe it continues to head. PepsiCo's line-up of waters, sports drinks, teas and energy drinks includes leading brands, and they illustrate how an advantaged portfolio of non-carbonated beverages can deliver great products for consumers, and solid returns for retailers and shareholders.

How are you preparing to grow PepsiCo's top line?

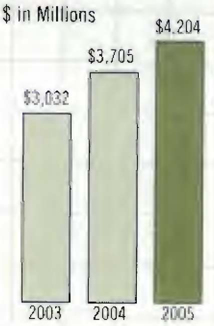
In a word, innovation — the lifeblood of any consumer products company. PepsiCo views this capability as a critical and sustainable competitive advantage. It is the reason we spend considerable time and dollars filling our pipeline with an array of consumer propositions to address needs for convenient foods and beverages.

We use a thoughtful and balanced approach to funding innovation and putting resources in place to support it. Some examples of that balance include balancing good-for-you and better-for-you product innovation with resources earmarked for our fun-for-you portfolio. In 2005, for example, our investment in new Aquafina FlavorSplash and new Gatorade Lemonade drove growth with our Smart Spot portfolio, while Lay's Cheddar and Sour Cream

Earnings Per Share*

Management Operating Cash Flow **

$ in Millions



* See page 76.
** See page 49.

U.S. Category Leaders

U.S. Category Leaders

flavored potato chips contributed to solid growth with our Lay's brand.

But it also means balancing investment between carbonated and non-carbonated beverages, and balancing between "close-in" ideas like line extensions, and entirely new product platforms that don't exist today. We've implemented new ways of coordinating the collection of insights from consumers and retail partners so we can better share those insights across our businesses, and generate ideas that have a greater chance of success in the marketplace.

I think it's important to understand that innovation isn't limited to products. Across PepsiCo, we're constantly innovating to strengthen our go-to-market systems and to find structures that drive faster, more efficient and more cost-effective decision making. A current example is our Business Process Transformation, or BPT, a comprehensive, multi-year initiative that centers on moving all of PepsiCo to a common set of processes for key business activities, with current efforts focused on North America.

More than a year ago, you announced PepsiCo's Business Process Transformation (BPT) initiative. What are the objectives of this program, and what is its status?

Through larger acquisitions and mergers over the years, such as Tropicana and Quaker, we've recognized the need to seamlessly integrate formerly independent information systems. We're also committed to harmonizing key business processes such as Finance, Consumer Insights, Purchasing and Supply Chain and continuously improving our customer service.

We're supporting these processes with common Information Technology applications, linking our systems so that key pieces of data supporting all our businesses flow seamlessly from system to system. 2005 was a big year of preparation for the first deployment of our new, integrated system, which started its phased roll out in early 2006.

In fact, on January 16, the very first of these new capabilities began its roll out. Several of our North American plants, along with our Global Procurement team, now have streamlined tools and processes used for purchasing materials other than commodities, packaging and ingredients. Additional capabilities will be rolled out over the next several years.

When complete, we expect to have an infrastructure that will support better, faster decisions, allowing us to capture more growth opportunities, and better serve our customers. Importantly, it will also leverage PepsiCo's scale for efficiency and effectiveness.

On the cost side, a number of key commodities have seen high rates of inflation. How is PepsiCo managing in an environment of increasing costs?

There is no doubt that 2005 was a challenging year for input costs — especially energy and plastics resin. Between several major hurricanes hitting the United States and inflation, we saw some expected and some unexpected pressure on our margins, but we managed those cost pressures and met our financial targets.

And we expect 2006 to be challenging as well, largely reflecting increased energy and commodity costs. However, we have solid plans in place to offset these rising costs through productivity programs and hedging strategies, and expect to carefully manage pricing to help offset some of the inflation.

PepsiCo's businesses generate a great deal of cash, and the Company's balance sheet is very conservative. Why don't you put more debt on the balance sheet and use the proceeds to increase the dividend or increase share repurchases?

PepsiCo does generate considerable cash, and we are disciplined about how cash is reinvested in the business. Over the past three years, $5.7 billion has been reinvested in the businesses through capital expenditures and acquisitions, and $12.0 billion has been returned to shareholders through a combination of dividends and share repurchases. In essence, any cash we have not reinvested in the business has been returned to our shareholders. And, we are pleased with our current capital structure and debt ratings, which give us ready access to capital markets and keep our cost of borrowing down.

PepsiCo's focus on people — specifically diversity and inclusion — has been a priority in previous reports. What results have you delivered through this focus and what changes have you made?

In terms of the diversity of our workforce, we've seen a significant increase in the number of women and people of color who've joined PepsiCo in various functions and at various levels. Since 2000, the percentage of women in management positions in the United States has risen from 20% to 25%. The number of people of color in management positions has climbed from 15% to almost 22% — we made a gain of about 2 points of growth in 2005 alone. This change in the workforce has contributed to our growth through product ideas, greater insights about consumers and connections into growing urban and ethnic communities.

While a diverse workforce is important, we must also create an inclusive environment where everyone — regardless of race, gender, physical ability or sexual orientation — feels valued, engaged, and wants to be part of our growth. It is only through

inclusion that we will fully unleash innovation and growth for our business.

To capture this potential, we made some changes in 2005. For example, to put accountability for diversity and inclusion squarely in the hands of our people, and into our divisions, we formed the PepsiCo Diversity & Inclusion Governance Council. Representatives from each division and various functions comprise the council, and its chair reports directly to me.

I also asked each of my direct reports to take ownership for the development of specific employee groups. Whether it is African Americans, Latinos, white males, women, or other groups of PepsiCo employees, each has a voice at the most senior decision-making entity at your company.

In the context of people issues, corporate responsibility is a hot topic. How are you ensuring PepsiCo associates are acting in accordance with the law, and — beyond the law — doing the right thing?

The need for trust between corporations and the general public is as big as ever, and investors rightly should ask this question of every company. PepsiCo's focus on values remains honed on a commitment to every shareholder — to deliver sustained growth, through empowered people, operating with responsibility and building trust.

This commitment, along with six guiding principles (found on page 7), is what we aspire to each and every day. It complements our approach to corporate governance, the strength of our financial controls, and the company's Worldwide Code of Conduct.

Our Values and our Worldwide Code of Conduct are known to every PepsiCo associate and are presented in 38 languages on our website (www.pepsico.com). But the strength of any such commitment is not in the words themselves, but in how they are lived every day.

We continuously remind our associates of the rewards that come with running the company in a legal, ethical and responsible way, along with the consequences of failing to do so. We want, and intend to be, a sustainable enterprise, and that demands our people act in responsible ways, and think about our businesses for the long term.

As we have with previous reports, we've included a section on corporate social responsibility to highlight what we've accomplished in 2005, and I invite you to visit our website as well to read our report in detail.

More importantly, I hope the contents of this annual report — along with even more details that are published on our website — will help you understand that your company is addressing the challenges ahead with the strength of muscular brands, a growing and powerful go-to-market system, a commitment to innovation, and passionate, diverse people committed to growing the business in responsible ways.

This is the PepsiCo that is poised to deliver on our commitment to responsible growth at any time, and on any day.

Steve

Steve Reinemund
Chairman and Chief Executive Officer

U.S. Category Leaders

A Word of Thanks to Sol Trujillo

Sol Trujillo retired from the board when he was named chief executive officer of Telstra Corporation, the Australian telecommunications and information services company. Sol served for five years on our Board, providing valuable insights and advice. He has an astute understanding of consumers and provided excellent guidance during our merger with Quaker. His counsel and contributions will be greatly missed.

Welcome to New Board Members

Joining our Board of Directors in 2005 were Dina Dublon, Victor J. Dzau, M.D. and Alberto Ibargüen.

Dina Dublon was, until October 2004, executive vice president and chief financial officer for JPMorgan Chase, the U.S.-based banking company with more than $1 trillion in assets. She brings a deep expertise in financial management that significantly enhances PepsiCo's capability in this important area. She will serve on our Audit Committee.

Dr. Dzau is one of the world's foremost authorities on health issues, chancellor for health affairs at Duke University and president and chief executive officer of the Duke University Health System. His medical insights and business acumen will be invaluable as we strive to achieve our commitment to health and wellness.

Alberto Ibargüen previously was chairman of the Miami Herald Publishing Company, a Knight Ridder subsidiary, and has served as publisher of the Miami Herald and El Nuevo Herald. In July 2005, he became president and chief executive officer of the John S. and James L. Knight Foundation, a major supporter of journalism programs and civic advancement. He brings both business and community expertise and will serve on the Audit Committee.

— SSR

OUR COMMITMENT

to deliver

SUSTAINED GROWTH

through

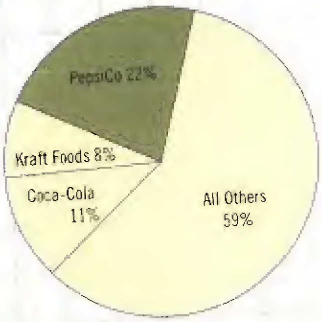
EMPOWERED PEOPLE

acting with

RESPONSIBILITY and building TRUST

U.S. Convenient Food and Beverage Sales

% Total Dollar Sales Snacks and Beverages



PepsiCo is the leading convenient food and beverage company in the United States.

GROWTH

Growth is our reason for being. In fact, growth is so much a part of PepsiCo's DNA that it's reflected in our values as our commitment to sustained growth.

Fundamentally, there are two ways for a corporation to generate profitable growth for its shareholders: by increasing revenues and decreasing costs.

It's a relatively simple concept, but the longer a company is in business and the bigger it gets, the more difficult growth is to achieve. And in accomplishing these most basic — and difficult — priorities over time, the single biggest contributor to sustained growth lies in how the enterprise consistently delivers top-line growth and bottom-line performance. Over time, the way a company delivers growth will define the difference between its success and failure.

PepsiCo Values

"Sustained Growth" means consistent growth for our business as well as our people — growth year after year.

"Empowered People" is the second piece of that commitment, as the decisions that drive the business come from tens of thousands of PepsiCo associates throughout the world who develop, manufacture and deliver our products. Empowered people act and think in ways that get the job done, and innovate to find new ways to achieve growth.

"Responsibility and Trust" is the third piece of our commitment. It articulates that acting responsibly and earning the trust of our shareholders, customers, consumers and other stakeholders is a necessity for growth. Our growth must come the right way. It takes a lifetime to build that trust, and a single misstep can destroy it. Winning is only worth it if is done the right way — acting in a responsible way that will build trust.

Our Competitive Advantages:

Strong brands.

World-class innovation.

Powerful Go-to-Market systems.

Top Line: Our Competitive Advantages

Growing revenues, or the top line, requires constant care and investment in our competitive advantages. These are the strengths we bring to the marketplace that set us apart. These include our quality brands — products known and trusted by consumers around the world. We constantly revitalize these brands with packaging and product improvements and consumer promotions to keep them strong.

When an opportunity to add new products that complement our portfolio comes along, we consider building them from within or acquiring new brands through smaller "tuck in" acquisitions, which can be integrated easily with our lines of business.

Our ability to innovate is another competitive advantage. We look for opportunities to capitalize on the value of our brands by creating new products and varieties. By innovating to meet consumer needs and preferences, we fill

consumption gaps and contribute to creating both healthier and indulgent choices for consumers, and bringing more enjoyment to their lives.

Bringing those products to consumers is where our third major competitive strength comes into play: our strong, established delivery systems. They include direct-store-delivery, where our own associates load and set up the shelves; warehouse systems, where retailers store and replenish product; and dedicated teams to supply foodservice and vending customers. The strength and span of our systems help us quickly introduce a product into the market — which helps us put our products within easy reach whenever a consumer is thirsty or hungry.

Bottom Line: A Constant Focus

Through our Business Process Transformation initiative, we are equally focused on reducing expenses to produce a healthy bottom line. We're streamlining our processes by employing new technology to meet customer and business needs. We're finding new ways to capture the full value of every penny we earn, such as using a new treasury management program to invest revenues the same day we receive them. We're consolidating our purchasing to secure more favorable prices and delivery. We're developing state-of-the-art water programs, energy conservation methods and other environmental initiatives that will make our businesses more sustainable.

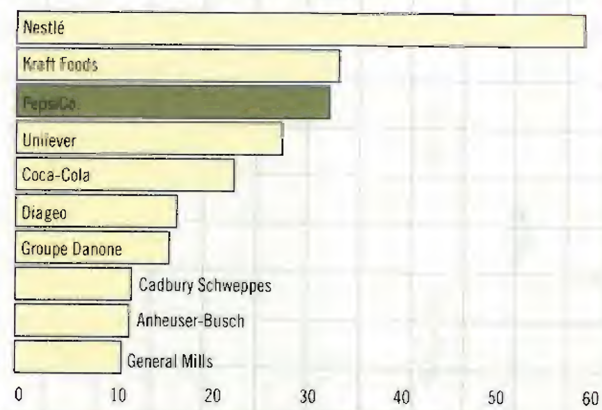
None of this would happen without our people, the drivers of everything we do. They are among the most talented and dedicated individuals in the world.

Each of these competitive strengths comes together to meet the needs of our consumers, shareholders and other stakeholders in creating sustainable growth on any day.

Top Branded Food and Beverage Manufacturers

$ Net Sales in Billions

Food and Beverage sales. Excludes food ingredients, pet and agricultural products. Includes fruit and dairy.



PepsiCo is the world's third largest food and beverage company.

PEPSICO VALUES

GUIDING PRINCIPLES

Care for customers, consumers and the world we live in

Sell only products we can be proud of

Speak with truth and candor

Balance short term and long term

Win with diversity and inclusion

Respect others and succeed together

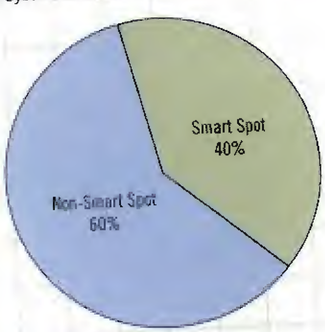
HEALTH & WELLNESS

Health and wellness represents one of our most critical opportunities for growth. In capturing this opportunity, we believe we can play a role in empowering and motivating consumers to lead healthier lifestyles, and we believe our actions are making a difference.

Our focus on product reformulation — reducing sugar, fat or sodium or adding whole grains and healthier oils; our commitment to developing new products that support healthier eating; and our passion for promoting active lifestyles, all illustrate our drive to make it easier for our consumers to make choices that are part of healthier lifestyles. In 2005, we became the first major food and beverage company to promote healthier lifestyles — beyond products — to consumers through a major program called S.M.A.R.T., which encourages healthier eating and exercise habits.

We realize that doing the right thing for our consumers and employees is doing the right thing for our business. In fact, our Smart Spot eligible products revenue grew more than two-and-one-half times faster than the rest of our portfolio in 2005. The Smart Spot symbol helps consumers find our products that can contribute to healthier lifestyles.

PepsiCo North America Revenues from Smart Spot Eligible Products
% System Revenue



A wide variety of PepsiCo products carry the Smart Spot symbol to identify choices that can contribute to healthier lifestyles.

Energy Balance

The solution to the problem of increasing obesity rates is far from simple. It requires consumers to understand and achieve energy balance — the balance between calories consumed and calories expended through activity. To help consumers achieve energy balance, we're providing them with convenient, healthier products they want to consume and that fit their busy lifestyles. We also are encouraging them to engage in physical activities they enjoy.

Our Commitment to Healthier Choices

Building on the foundation of brands like Quaker, Tropicana, Aquafina, Baked! and others, we're putting more emphasis on making products with healthy ingredients — like oatmeal, water and juice — more convenient. For example, we've combined fruit and juice and made them more convenient through Tropicana FruitWise, a delicious line of fruit strips, bars and beverages that deliver one to two servings of fruit in a portable, convenient form.

Our Quaker Milk Chillers product is another example. These dairy products have reduced calories and are fortified with calcium and seven essential vitamins. Other examples include:

- Eliminating trans fats from Frito-Lay branded products in 2003. We were the first major food company to make this change.
- Creating new reduced-sugar Instant Quaker Oatmeal varieties, and adding Take Heart and Weight Control versions to our instant oatmeal line-up.
- Creating Tropicana Light 'n Healthy orange juice beverage, which has half the sugar and calories of orange juice.
- Adding a new variety of flavored water to our Aquafina line-up with the introduction of FlavorSplash. This non-carbonated variety gives consumers a hint of flavor in their water, without adding calories.
- Building on the success of Propel Fitness Water with the introduction of Propel Calcium, the first national fitness water with added calcium.

Energy Balance = calories in - calories out

Smart Spot Products Contribute to Healthier Choices

In 2004, PepsiCo launched the Smart Spot symbol, the first-of-its-kind designation that makes it easier for consumers to identify PepsiCo products which can contribute to healthier lifestyles. And in 2005, our Canadian business introduced a similar program to consumers.

Products with the Smart Spot designation in the United States meet nutrition criteria based on authoritative statements from the U.S. Food and Drug Administration (FDA) and the National Academy of Sciences. Those criteria define limits for fat — including saturated and trans fats — cholesterol, added sugar and sodium. The criteria also are used to identify products formulated to have specific health or wellness benefits, or products reduced in calories or ingredients such as fat or sugar. For more information visit www.smartspot.com.

Our Commitment to Promoting Healthier Lifestyles

As a leading food and beverage company, we believe we have a role in supporting programs that help consumers with the "calories out" side of the equation as well.

The PepsiCo S.M.A.R.T. lifestyle program involves five simple steps for healthier living. The S.M.A.R.T. program is supported with a national advertising campaign. And in 2006, PepsiCo plans to build 12 Smart Spot playgrounds in inner city locations across the county. Our goal is to support more active lifestyles for families and kids — and get them to "move more."

SMART CHOICES MADE EASY

Impacting Local Communities

PepsiCo is proud to be the national presenting sponsor of America On the Move (AOM), a national program dedicated to helping individuals, families and communities make positive changes to health and quality of life. AOM recommends taking 2,000 more steps and consuming 100 fewer calories a day to stop weight gain.

Working with AOM, PepsiCo has partnered with the National Urban League and the National Council of La Raza to address common health concerns that affect African Americans and Latinos. Both organizations are tailoring AOM's approach to help people initiate and maintain meaningful and measurable behavior changes that support healthy eating and active living habits.

In Mexico, the PepsiCo Foundation has partnered with Fundación Actívate to pilot Activa2, an energy balance program for youth which encourages healthy eating habits and exercise.

Our Commitment to Schools and Educators

Schools want to provide children with the right food and beverage choices, too. That's why PepsiCo provides a wide range of offerings in schools, including Smart Spot products in particular. New products that are appropriate for kids are being introduced first in schools — products like reduced-fat Baked! Cheetos snacks. We are working with our bottlers and vending distributors to establish guidelines on school offerings, again with an emphasis on Smart Spot products.

To help educate kids about energy balance, PepsiCo and America On the Move developed a lesson plan called Balance First. This program reached 3 million elementary age students in 2004. In 2005, we continued to distribute the lesson plans to elementary schools. And in partnership with Discovery Education, we've distributed the Balance First program to 15,000 middle schools in the United States — virtually every middle school in the nation.

In partnership with the American Beverage Association, PepsiCo and other industry members developed a school vending policy aimed at providing lower-calorie and/or nutritious beverages and limiting the availability of soft drinks in schools.

Children in Washington DC say thank you for their new Smart Spot playground.

Start with a healthy breakfast
Move more
Add more fruits, veggies & whole grains
Remember to hydrate
Try lower calories or fat

PepsiCo estimated worldwide retail sales: $85 billion

INNOVATION

Whether it's a new product, improvement to an existing product, new packaging or a unique promotion, we're relentless in our drive to keep our products relevant to consumers.

March of New Products

Early in the year, Pepsi-Cola North America capitalized on our leading Aquafina brand with FlavorSplash, a zero-calorie water made with natural fruit flavors and sweetened with Splenda no-calorie sweetener.

Our SoBe team built on the strength of its South Beach Diet program-endorsed Lean line with two new flavors: Lean Energy and Lean Mango Melon. The Pepsi-Lipton Tea Partnership unveiled a new Diet Sweet version of ready-to-drink Lipton Iced Tea.

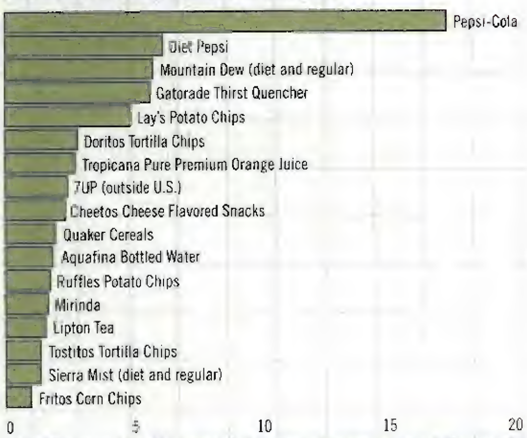
We also kept our carbonated soft drink brands top of mind. Building sales of our flagship Pepsi brand, Pepsi-Cola introduced Pepsi Lime and Diet Pepsi Lime, a pair of colas featuring the popular lime flavor. Pioneering a new category of "energy sodas," Pepsi-Cola launched MDX, a beverage touting the familiar citrus flavor of Mountain Dew, but fueled by a "power pack" of ingredients including ginseng, guarana, taurine and D-ribose.

The march of our new products continued when Tropicana introduced Tropicana Pure Premium Essentials with Fiber — the first national orange juice with added fiber. It delivers as much fiber as a whole orange in every 8-ounce glass. Then we gave lemonade a new meaning with the introduction of a Gatorade Lemonade, a line that combines the refreshing taste of lemonade with the scientifically supported formula of Gatorade Thirst Quencher.

At Frito-Lay North America, we reformulated all our Quaker Chewy granola bars to remove trans fat — plus we reformulated many of them to reduce sugar by 25% and add calcium. Many of these bars now bear the Smart Spot symbol and our new package graphics reinforce the linkage to Quaker Oatmeal. In our Oberto meat snacks line, distributed by Frito-Lay, we introduced Oh Boy! Oberto Beef Jerky Crisps, a first-of-its-kind snack that bridges the gap between beef jerky and traditional snack chips.

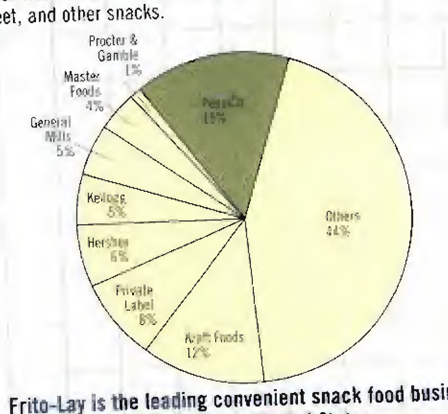
At our Quaker Foods business, we added to our successful Life Cereal line with the introduction of Life Vanilla Yogurt Crunch — combining Life Cereal with yogurt-coated clusters while delivering nine essential vitamins and minerals and providing a good source of calcium and fiber. Quaker also introduced new Weight Control instant oatmeal, a quick, convenient way to eat a nutritious breakfast that is high in fiber and a good source of protein, and Quaker Oatmeal-To-Go bars, which provide all the nutrition of a bowl of instant oatmeal.

Largest PepsiCo Brands
Estimated Worldwide Retail Sales $ in Billions



PepsiCo now has 17 powerful brands known around the world that each generate annual retail sales of more than $1 billion.

U.S. Convenient Foods Sales
% Retail Sales in Measured Channels.
Includes chips, pretzels, ready-to-eat popcorn, crackers, dips, snack nuts/seeds, meat snacks, yogurt, bars, cookies, pastry, sweet, and other snacks.



Frito-Lay is the leading convenient snack food business in measured channels in the United States.

Hundreds of innovations help drive our growth in international markets. Pepsi Cino, the first cola-coffee flavor combination from a major beverage company, was a dynamic new entry to the carbonated soft drink arena. 7UP H2O, a sugar-free sparkling water infused with the flavor of 7UP, was launched in Argentina and proved highly appealing to consumers interested in lighter beverages. In China, the relaunch and expansion of Gatorade helped us capture a solid position in the growing sports drink category. And we expanded Tropicana in Europe, Asia and the Middle East.

Capturing Consumer Attention with Packaging

Packaging captures attention and gives us an opportunity to tell consumers about our brands. For example, Lipton Original received a makeover. It's now in 16-ounce glass bottles that include a logo noting the brand's naturally protective antioxidants. We introduced new striking black and silver graphics to highlight reformulated Pepsi ONE.

SoBe Beverages celebrated its tenth anniversary by unveiling new graphics for the entire 20-ounce product line, scheduled to be on the shelves in 2006. The Tropicana Light 'n Healthy packaging was the first juice beverages to carry Weight Watchers' proprietary *POINTS* values on the packaging.

Outside the United States, one highlight of our packaging innovation was a new 7UP plastic bottle with a distinctive, proprietary shape that features bold graphics and is attracting lots of attention on store shelves.

Promotions that Keep Our Brands Top of Mind

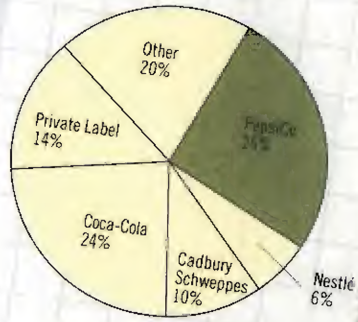
Pepsi-Cola used music to help keep our brands top of mind. The Pepsi iTunes giveaway offered 200 million free songs. In mid-year, Pepsi and Yahoo! announced a partnership to bring music to fans with "Smash on Yahoo! Music," an adaptation of the "Pepsi Smash" summer concert TV program.

With "Call Upon Yoda," an instant-win sweepstakes, Pepsi-Cola took advantage of the release of the highly anticipated movie "Star Wars: Episode III, Revenge of the Sith." Frito-Lay joined by launching Star Wars-inspired Twisted Cheetos snacks, which temporarily turned the color of consumers' tongues into "Yoda Green" or "Darth Vader Dark."

Pepsi was back with our "Go Pro" sweepstakes, a sports fan's fantasy that offered the chance to win trips to select professional sporting events across the country. Then Pepsi turned up the volume even higher with its highly successful Mountain Dew promotion that gave away an Xbox 360 next-generation video game and entertainment system every ten minutes.

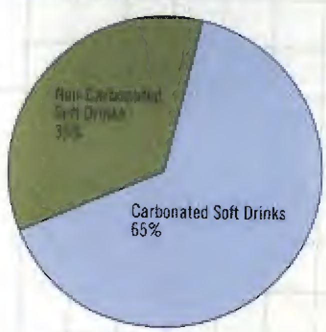
Mountain Dew made news with Mountain Dew (MD) Films and Universal Pictures joint release of "First Descent," the story of the rise of snowboarding. Our SoBe business kept the action going all year with concert tours, support of major surfing events, supercross/motocross racing and skateboarding — activities that reflect active lives of "Team Lizard" fans. Gatorade gave its brands local visibility through the Gatorade Athlete of the Year award program which recognizes young athletes.

U.S. Liquid Refreshment Beverage Market Share
% Volume in Measured Channels



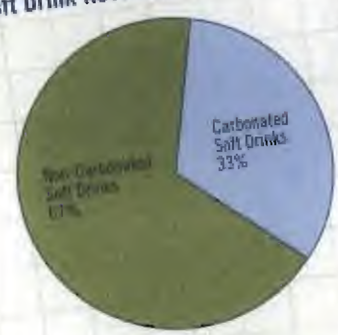
PepsiCo has the leading share of the liquid refreshment beverage market.

PepsiCo Beverages North America Carbonated Soft Drink Volume vs. Non-Carbonated Soft Drink Volume



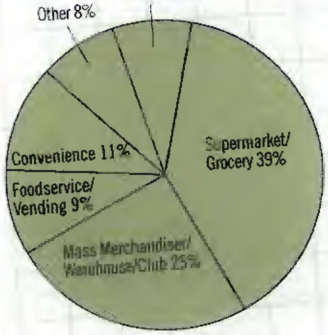
Carbonated soft drinks generate the largest volumes.

PepsiCo Beverages North America Carbonated Soft Drink Revenue vs. Non-Carbonated Soft Drink Revenue



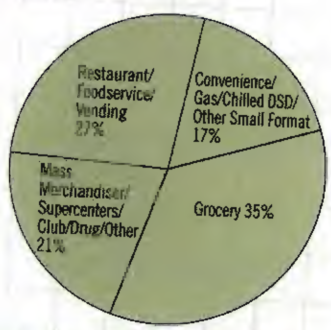
Non-carbonated soft drinks generate the largest revenue.

U.S. Frito-Lay North America Distribution Channels
% Volume



Frito-Lay North America distributes to some 430,000 retail outlets each week.

U.S. PepsiCo Beverage Distribution Channels
% Volume



PepsiCo beverages are distributed by a powerful go-to-market system which includes company-owned operations, independently-owned franchised bottlers and warehouse delivery systems.

EXECUTION

Our goal is to have our products in arm's reach whenever and wherever consumers want them. And we're delivering — literally. For example, our brands include seven of the 13 largest food and beverage brands sold in U.S. supermarkets. Whether they're new or brand-loyal consumers, each consumer must be able to find our products in order to buy them. That's why the strength of our selling, distribution and internal systems is so critical.

From stocking shelves and creating displays in supermarkets, to making sure the small corner deli has our products, our front-line teams go the distance. They are supported by an infrastructure dedicated to streamlining our processes and enhancing our growth through efficiency. For example, we are consolidating global purchasing to ensure we leverage our spending, and we are revamping our business processes to give our customers what they need.

Our Distribution Systems

Most of our sales are delivered through direct-store-delivery (DSD) distribution systems, where a dedicated team delivers the product to the stores and places our products on the shelves. This gives us the opportunity to merchandise our products and make sure they are always available. It gives the route salesperson the ability to meet the specific needs of any retailer. Our system reached hundreds of thousands of retail outlets this way, from tiny convenience stores to the largest supermarkets, helping us distribute new product offerings in record time. In 2005, we started to add 475 new distribution routes at Frito-Lay in the United States — our largest addition in nearly a decade. Internationally, our sales force of almost 35,000 reaches nearly every corner of the globe.

Our Gatorade and shelf-stable Tropicana juices, as well as many of our Quaker and other less perishable products, are delivered through one of the largest warehouse delivery systems in the world. Tropicana Pure Premium comes fresh through a refrigerated warehouse or chilled direct-store-delivery system.

Our distribution systems are designed to meet the needs of our customers. For example, Frito-Lay sells its Gamesa cookies and crackers through warehouse, third-party distributors, direct shipment and DSD. When taken together, over the past three years, PepsiCo products delivered through all these methods contributed more to the growth in U.S. supermarkets than any other company.

An equally robust system is dedicated to delivering our products to foodservice and vending customers. New beverage partners include Taco John's and Arby's — high-traffic restaurants. Taco John's operates and franchises more than 400 quick-serve restaurants in 27 states. Arby's consists of nearly 3,500 restaurants worldwide, including more than 1,000 in the United States. Pepsi-Cola expanded its partnership with Metromedia Restaurant Group (MRG), which has more than 800 restaurants. The new partnership adds Bennigan's and Steak & Ale restaurants to the existing relationship with Ponderosa and Bonanza Steakhouses.

Our distribution systems

Direct-store-delivery

Broker-warehouse

Foodservice and vending

Business Process Transformation/Project One Up

Execution begins long before our products are delivered. PepsiCo's Business Process Transformation (BPT) initiative is addressing the changing market and needs of our customers. In the past, PepsiCo divisions operated on separate information systems and had varying business processes. In 2004, we embarked on a journey to change our business model to better meet the needs of our retail customers. The most central piece of our BPT efforts is an implementation called Project One Up, so named because it will allow us to "one up" the competition. It's a multi-year project to simplify and synchronize our business processes and tools into one common platform.

We believe Project One Up will help PepsiCo in key areas:

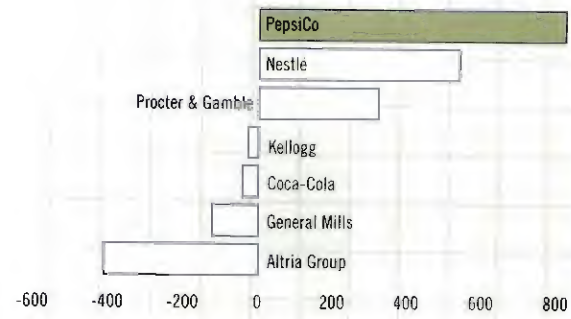
- Customer insights — We will collect more and better consumer behavior and marketing insights to increase sales.
- Procurement — We will consolidate and optimize purchasing to reduce costs and ensure supply.
- Supply chain — We will manufacture and distribute our products faster and more efficiently, based on the increased information and new processes.
- Finance — We will consolidate billing and provide more complete and responsive financial data to our trading partners.
- Go-to-market — We will share information throughout PepsiCo faster and with more efficiency, improving customer service.

We have a dedicated team of representatives from various divisions and functions working on Project One Up.

Making Every Penny Count

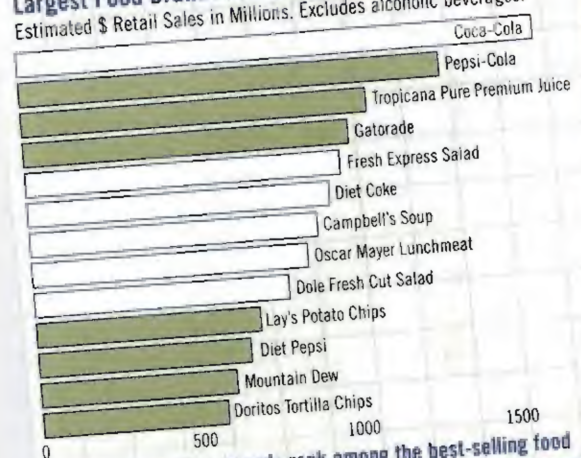
nnovation can improve our processes. When our treasury team required a banking system with global visibility to optimize PepsiCo's investments, they eamed with Citigroup to develop a web-based tool called "TreasuryVision" that provides views of real-time balances, cash positions, investments and borrowings worldwide. Every day, in countries around the world, our sales force receives payments from stores for products and deposits those funds across hundreds of bank accounts. In the past, there may have been a lag of up to several days before our treasury team had access to these funds. The new system will provide visibility to these funds and will enable us to invest them more efficiently.

Top Contributors to U.S. Supermarket Growth
$ Retail Sales in Millions 2002-2005



During the period from 2002 to 2005, PepsiCo was the largest contributor to U.S. supermarket growth.

Largest Food Brands in U.S. Supermarkets
Estimated $ Retail Sales in Millions. Excludes alcoholic beverages.



Seven of PepsiCo's brands rank among the best-selling food and beverage brands in U.S. supermarkets. No other company comes close.

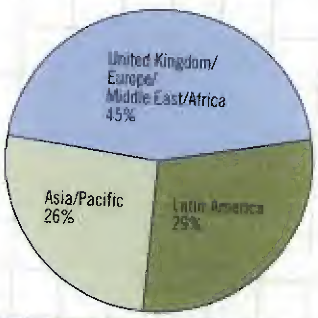
International growth is our single largest opportunity.

INTERNATIONAL

With 95% of the world's population located outside North America, international growth is our single largest opportunity. Our strategies are focused:

- Build on our snack leadership position.
- Focus on the strengths of our beverages.
- Grow through acquisitions.
- Take advantage of our scale.

PepsiCo Beverage Volume Outside North America
% System Volume by Region
Includes Pepsi-Cola, 7UP, Gatorade, Tropicana and other beverages.



PepsiCo beverages are distributed locally by company-owned and franchised bottlers.

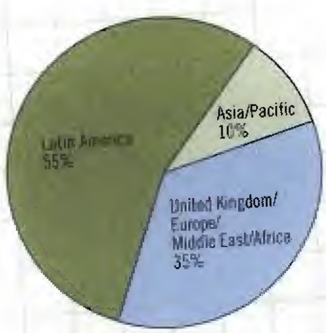
Build on Our Snack Leadership Position

Our snack business is the largest in the world, and our brands are recognized in markets ranging from Mexico to the United Kingdom to Thailand. Yet, in some of the largest developing markets, such as China and India, per-capita consumption is still small and many consumers have never tasted our brands. To us, that means vast opportunities.

We're building our existing business by offering consumers more variety and convenience, including flavors tailored to local tastes. For example, in China we offer Lay's potato chips in flavors that include Hangzhou Stewed Meat, Hokkaido Crab and Cool Cucumber.

Providing products and programs that address consumers' growing interest in health and wellness also drives our success. In the United Kingdom, we lowered the saturated fat in our standard Walkers crisps by 70% and launched Potato Heads, a highly successful range of crisps for children, also with 70% less saturated fat and no artificial flavors or preservatives. In Mexico, we have driven strong growth of the healthy segment with brands such as Nutritas, an extruded snack, and Sun Chips multigrain snacks.

PepsiCo Snack Volume Outside North America
% System Volume by Region



PepsiCo has the largest snack business in the world.

Focus on the Strengths of Our Beverages

Our international beverage volume has grown consistently during the past four years. Through our company-owned and franchise-owned bottlers, we make and market an array of major brands, including Pepsi-Cola, 7UP, Mirinda and Mountain Dew. Our portfolio also includes various local soft drink brands.

We work relentlessly to keep our brands strong, exciting and locally relevant, with a continuous flow of product news and package innovations, and exciting marketing programs — often leveraging the universal appeal of music and sports.

We also offer consumers a portfolio of non-carbonated beverages that includes our Gatorade, Tropicana and Aquafina brands, as well as Lipton teas through our joint venture with Unilever. Tropicana is now available in more than 30 countries and we've expanded the presence of Gatorade, the world's leading sports drink, into markets such as China and India.

Grow through Acquisitions

Acquisitions offer additional opportunities to build our business and enter new markets and categories. We now have full ownership of Snack Ventures Europe, Continental

PepsiCo products are available in more than 200 countries and territories.

Europe's largest snack food company, with operations in Holland, France, Belgium, Spain, Portugal, Greece, the Baltics, Hungary and Russia.

Adding Star Foods to our portfolio strengthened our position as Poland's market leader in potato chips and gave us the largest position in the broader savory snack category, which includes potato chips, pretzels, nuts and extruded snacks.

We also acquired Sakata Australia, the market leader in rice snacks. This allows us to offer a wider array of choices in "better-for-you" snacks to consumers in Australia and other countries.

In Germany, we expanded and strengthened our beverage portfolio with the acquisition of Punica Getränke GmbH, a leading maker of fruit juices and juice drinks. The purchase dramatically expanded our juice business in continental Europe.

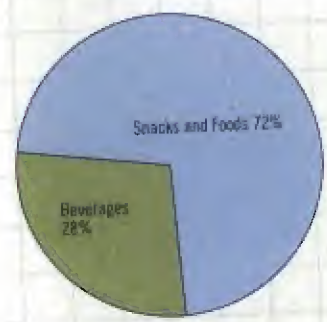
In the Netherlands, Belgium and France, we are waiting for regulatory approval to complete the acquisition of Sara Lee Corporation's European nut business in these countries, to further expand our market presence.

Take Advantage of Our Scale

We continually seek opportunities to take greater advantage of the combined scale of our business. For example, in the United Kingdom we have Power of One teams calling on customers to offer both beverages and snacks. In Mexico, we conduct joint promotions that include both Pepsi products and Sabritas snacks. And, in many parts of the world, we have merged our snack and beverage organizations to operate more efficiently, broadening the skills of our people and encouraging cross-business sharing of ideas.

Coordinated purchasing has driven substantial productivity gains; we buy through PepsiCo's Global Procurement group for strategic materials and through regional procurement systems where it makes more sense to source locally. This has contributed to steady improvement in operating margins since 2002.

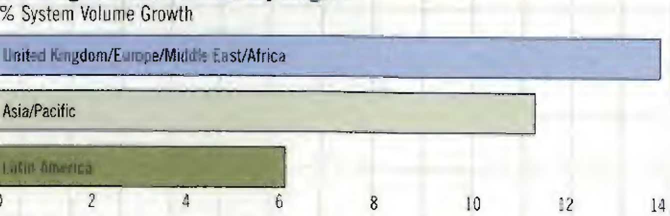
Net Revenues Outside North America
% Net Revenues



Nearly three-fourths of PepsiCo International revenues are generated by snacks and foods.

Snack Volume Growth by Region
% System Volume Growth

Beverage Volume Growth by Region
% System Volume Growth



PepsiCo International beverages and snacks generated growth across all regions.

Our Sustainability Vision

PepsiCo's responsibility is to continually improve all aspects of the world in which we operate — environment, social, economic — creating a better tomorrow than today.

Tomorrow > Today

Focus Areas

- Values
- Diversity and Inclusion
- Health and Wellness
- Water
- Packaging

SUSTAINABILITY

Sustainability lives at the intersection of public and business interests. It encompasses citizenship and corporate social responsibility, which are about doing the right things for society and for the business. It encompasses the health of the corporation, which is about fulfilling our mission of creating financial rewards and growth.

A History of Responsibility

PepsiCo has always been a responsible corporation. Our Worldwide Code of Conduct had guided our actions for decades, and we have been a consistent contributor to our communities and to the nonprofit organizations that support our society. We have been recognized as a leading company in areas such as diversity and inclusion, purchasing from women-owned and minority-owned suppliers, corporate governance, environmental stewardship and social leadership. We provide our associates with a broad menu of benefits and competitive compensation. We recognize our responsibility to consumers to provide safe, quality products, and to offer product choices that help them meet their needs, whether it is a need for pure refreshment and fun, or for foods and beverages that make it easier and more enjoyable for them to lead healthier lives.

We recognize that is not enough.

Our Sustainability Journey

In 2003, we took the first steps on a journey to become a more sustainable corporation. We voluntarily adopted the Global Reporting Initiative (GRI) guidelines as a template for reporting on our economic, environmental and social performance — the "triple bottom line" — and a measure of our sustainability. In 2004, we took another important step with the establishment of our Sustainability Task Force, comprised of senior executives from all our divisions.

Throughout 2004 and 2005, the Sustainability Task Force defined our sustainability vision and we determined our key focus areas: values, diversity and inclusion, health and wellness, and the environment, especially water and packaging. We placed emphasis on the development of environmental standards and metrics.

The Sustainability Task Force, working with PepsiCo's Environmental Task Force, developed consistent metrics for tracking our progress in the areas of water and energy. These measures are being introduced into all our divisions.

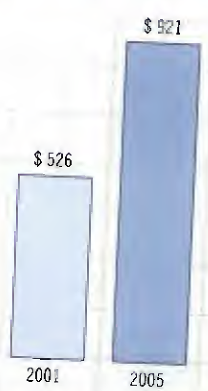
A sound Environmental Management System (EMS) is basic to sustainability. In 2005, PepsiCo developed a framework that establishes rigorous procedures for managing our environmental impacts. Previously, each division had distinct environmental programs and processes. We have targeted 2006 to begin the process of implementing our new EMS framework across our businesses.

Further progress was made on our Capital Expenditure Filter, a process that ensures that sustainability issues are formally considered in all major capital expenditure proposals. We piloted the filter on two projects, a new Gatorade plant in Virginia and a new warehouse in Arizona. The filter proved to be a valuable tool in decision-making,

Our Mission

We aspire to make PepsiCo the world's premier consumer products company, focused on convenient foods and beverages. We seek to produce healthy financial rewards for investors as we provide opportunities for growth and enrichment to our employees, our business partners and the communities in which we operate. And in everything we do, we strive to act with honesty, openness, fairness and integrity.

PepsiCo Supplier Diversity Spending
$ in Millions



Spending with women and minority suppliers has grown at a compounded annual rate of more than 15%.

Contribution Summary

PepsiCo Foundation	$21.6 Million
Corporate Contributions	4.3 Million
Divisions	3.7 Million
Estimated In-Kind Donations	20.8 Million
Total	$50.4 Million

The PepsiCo Foundation and PepsiCo committed $2.0 million in disaster relief related to the tsunami in Southeast Asia. The PepsiCo Foundation contributed $2.1 million in relief directed to victims of Hurricane Katrina. PepsiCo Foundation and PepsiCo committed $2.0 million in relief for Pakistan earthquake victims. The PepsiCo Foundation contributed $500,000 to establish water projects in China and another $385,000 for projects in India. In-kind donations include food, beverages, equipment and services at cost to PepsiCo.

Corporate Governance Recognized

Independent organizations rate companies on the quality of their corporate governance. For the fifth consecutive time, PepsiCo scored a 10 out of 10 rating from Governance Metrics International. Institutional Shareholders Services said PepsiCo outperformed 97.1% of the S&P 500 companies and 98.1% of the companies in the food, beverage and tobacco group.

helping us identify potential environmental impacts, such as watershed protection, green building design opportunities, renewable energy usage and biodiversity.

We are seeking opportunities to implement our minimization and optimization philosophy, both reducing our impacts and seeking ways to reach optimal solutions. For example, Gatorade is installing state-of-the-art high speed lines that minimize product spillage. The lines use advanced air rinsing of empty Gatorade bottles.

Values

Each year, every PepsiCo associate is asked to review our Worldwide Code of Conduct and recommit to living by it. Associates receive training in the Code, which is available in 38 languages and is accessible from both our internal and external websites. In 2005, we took additional steps to ensure that key associates understand every aspect of our Code. We developed online and written training and certification that approximately 25,000 executives and associates are required to complete. We report the results of these programs to our Board of Directors.

During the year, we improved our Speak Up line — a free hotline operated by a third party — which PepsiCo associates may call to report any issue of concern, including those relating to values, Code of Conduct and accounting and auditing issues. The line is accessible from anywhere around the world and callers may remain anonymous.

Diversity and Inclusion

We are becoming a much more diverse and global company. Actively working to create a more diverse workforce and supplier base helps us better understand customers and consumers. A focus on developing an inclusive atmosphere where all associates feel they can succeed helps PepsiCo succeed.

Each of our employee networks is represented at the most senior levels by an executive reporting to our chief executive officer. Our U.S. groups include African-Americans, Latinos, Asian, Women, White Males, Gay/Bisexual/Lesbian/Transgender (GBLT) and our newest group, "Enable," for individuals with different abilities.

We launched an electronic employee newsletter dedicated to diversity and inclusion. These new initiatives, plus ongoing programs and the continued counsel of our Ethnic Advisory Boards, are leading to better business insights and decisions.

Our program to increase spending with women and minority suppliers was in the spotlight when PepsiCo Chairman and Chief Executive Officer Steve Reinemund was named chairman of the National Minority Supplier Development Council (NMSDC).

We have about 157,000 associates worldwide

Selected Diversity & Inclusion Awards

- Hispanic Magazine: "100 Companies Providing the Most Opportunity for Hispanics."
- The National Association for Female Executives (NAFE): "NAFE 2005 Top 30 Companies for Executive Women."
- Latina Style Magazine: "50 Best Companies."
- New York Urban League: Corporate citizenship, hiring, supplier relations and philanthropic practices.
- DiversityInc: No. 1 for African Americans, No.1 for Latinos, No. 2 for Recruitment and Retention, No. 4 for Asian Americans, No. 5 for Gay/Lesbian employees, No. 8 for Supplier Diversity and No.4 for overall diversity.
- Women's Business Enterprise National Council: "America's Top Corporations for Women's Business Enterprises."
- The Hispanic Association on Corporate Responsibility: Corporate Index.
- 100% on the Human Rights Corporate Equality Index.
- Black Enterprise: "30 Best Companies for Diversity."
- FORTUNE magazine: Top employers for minorities.
- Black Collegian magazine: "Top 100 Diversity Employers."
- FORTUNE magazine: "Top Employers for Women."

U.S. Diversity and Inclusion Statistics

At Mid Year

	Total	Women	%	Minority	%
Board of Directors	14	4	29%	4	29%
Senior Managers	15	4	27%	3	20%
All Employees	60,634	16,029	26%	17,214	28%
All Managers	7,130	1,810	25%	1,550	22%

Our Board of Directors is pictured on page 21. Our Senior Managers are named on page 20.

In 2005, we increased the percentage of our women managers by one point and our minority managers by two points. Our international operations also made significant progress in achieving diversity goals with the number of women in executive positions increasing by more than 30% in 2005.

Employee Health and Wellness

Consumers are not the only beneficiaries of our focus on health and wellness. Our associates also reap the advantages. HealthRoads is our innovative wellness benefit offered in North America. The program promotes healthier lifestyles through a combination of personalized coaching, fitness and nutrition programs, online tools, resources and worksite wellness initiatives.

HealthRoads offers a variety of programs that encourage associates to improve their health. A Personal Health Assessment provides information tailored to the associate's unique health needs and recommends steps for improving health. The program includes initiatives such as America On the Move (AOM), weight management programs and 5 A-Day, a program where participants are encouraged to eat at least five servings of fruit and vegetables a day for better health.

Water

Water is a key sustainability priority for our company. We work closely with governments, municipalities and technical experts to make sure that our water practices are responsible. Over the years, we have voluntarily developed many programs to reduce, reuse and recycle water, and that commitment is stronger than ever. We also work proactively to improve water supplies in communities where quality or quantity is a problem. And we readily donate water when disasters strike.

Every PepsiCo division is engaged in water projects. In Europe and Asia, we harvest rainwater to help restore aquifers. In countries like India, where water shortages can be severe, we are building community infrastructure to help meet needs. In Kerala, India, for example, Pepsi-Cola increased the water supply for that drought-stricken community by digging new wells.

In the United States, our conservation efforts include reducing our use of water through conservation techniques, using recycled water for plant maintenance and using wastewater to irrigate crops used for animal feed.

In China, PepsiCo Foundation is partnering with China Women's Development Foundation (CWDF) — which is part of the All China Women's Federation — on a research and development initiative designed to expand availability of safe drinking water for the people of Western and Central China. In India, PepsiCo is providing support to the Energy and Resources Institute (TERI) to create sustainable state-of-the-art water resources management processes in the community.

Packaging

Packaging — particularly that of our beverage containers — is another key sustainability priority. PepsiCo fully supports the Environmental Protection Agency's (EPA) hierarchy: Reduce, Reuse, Recycle.

- Reduce: PepsiCo has reduced the weight of our beverage packaging significantly and uses nearly 60% less packaging now than in 1990 to deliver the same amount of soft drinks.
- Reuse: Our aluminum cans contain approximately 50% previously used aluminum materials. Our glass bottles contain between 25%-35% of previously used material. In 2002, PepsiCo committed to include 10% recycled content in

In South Africa, our Simba lion mascot helped build awareness of HIV/AIDS on World AIDS Day.

our carbonated soft drink plastic bottles in the United States by 2005. Thanks to our bottlers, PepsiCo met that goal on schedule.

Recycle: While beverage containers are the most recycled consumer packaging in the United States, we recognize that recovery rates need to increase. We helped found a new organization, the Beverage Product Environmental Council (BPEC), to increase beverage container recycling rates.

We continue to be careful stewards of our environment in other areas. For example, Tropicana minimizes waste by using every part of the orange as well as its by-products after juice is extracted. Frito-Lay recovers starch from potatoes for use in other industrial and food processes. Similarly, all our businesses are working to reduce, reuse and recycle throughout the manufacturing process.

In India, through an innovative partnership, PepsiCo has begun working with Exnora International and the Women's Self Help Groups, both non-governmental groups, and the Pammal Municipality on a collaborative venture to establish an infrastructure to manage household solid waste.

HIV/AIDS

Early in 2005, we announced a global HIV/AIDS policy. In South Africa, we introduced a company-sponsored program that offers full treatment. On World AIDS Day, our Simba lion mascot helped build awareness. We also focused on other high risk areas. In China, India, Russia and Thailand, workplace programs are underway building awareness, increasing prevention and improving access to information and care. For example, in China we kicked off a hotline to answer questions on HIV/AIDS in a safe and confidential manner. The hotline also provides information on qualified treatment facilities. Our business in Thailand was recognized by the Thai government for its work on HIV/AIDS.

GRI Report is Online

You may have noticed that this year we have not included our Global Reporting Initiative (GRI) report in this annual report. There are two reasons:

1. The report is increasing in size and complexity and including it in the annual report was less practical and efficient.
2. The vast quantities of paper required to produce a printed sustainability report seemed paradoxical. Putting our report online saves approximately 210 tons of wood from trees.*

This year, we will move to a web-based report. You will be able to find the report and more information on our activities on our corporate website www.pepsico.com under the GRI tab. We are reporting on new indicators, including providing our political and charitable contributions policies with detailed reports on these contributions. We are also updating our report on HIV/AIDS and other indicators as appropriate.

*Environmental impact estimates were made using Environmental Defense Paper Calculator. For more information, visit www.papercalculator.org.

Selected Awards

- Mexican Center for Philanthropy: Sabritas, our snack business in Mexico, is named a "Socially Responsible Business."
- Frito-Lay North America: Environmental Protection Agency (EPA) Star Partner of the Year Award for Leadership in Energy Management.
- National Business Group on Health: "Best Employers for Healthy Lifestyles."
- Frito-Lay distribution center in Rochester, NY: Certified by the U.S. Green Building Council and granted LEED (Leadership in Energy and Environmental Designs) Gold Status.
- Occupational Hazards magazine: "America's Safest Companies."
- AIDS Response Standard Organization: PepsiCo Thailand, "Certificate of Gold Level."
- California Waste Reduction Award Program (WRAP): Frito-Lay Modesto plant as a "Top 10 WRAP of the Year Winner."
- FORTUNE magazine: "America's Most Admired Companies."

Our CEO and CFO have issued the certifications required by the Securities and Exchange Commission (SEC) regarding the quality of PepsiCo's public disclosure. PepsiCo also has submitted its CEO certification as required by the New York Stock Exchange (NYSE).

Visit us on www.pepsico.com

Corporate Officers and Principal Divisions

Co-Founder of PepsiCo

Donald M. Kendall
Over 55 years of PepsiCo experience.

Corporate Officers

Steven S Reinemund
Chairman of the Board and
Chief Executive Officer
57. 21 years.

Indra K. Nooyi
President and Chief Financial Officer
50. 12 years.

Peter A. Bridgman
Senior Vice President and Controller
53. 20 years.

Albert P. Carey
President, PepsiCo Sales
54. 24 years.

James Kozlowski
Senior Vice President, Global Procurement
55. 20 years.

Tod J. MacKenzie
Senior Vice President,
Corporate Communications
48. 18 years.

Matthew M. McKenna
Senior Vice President, Finance
55. 12 years.

Margaret D. Moore
Senior Vice President, Human Resources
58. 32 years.

Lionel L. Nowell III
Senior Vice President and Treasurer
51. 6 years.

Clay G. Small
Senior Vice President,
Managing Attorney
56. 24 years.

Larry D. Thompson
Senior Vice President, Government Affairs,
General Counsel and Secretary
60. 1 year.

Principal Divisions and Officers

Frito-Lay North America
7701 Legacy Drive
Plano, TX 75024
972-334-7000

Irene B. Rosenfeld
Chairman and Chief Executive Officer
52. 1 year.

PepsiCo International
700 Anderson Hill Road
Purchase, NY 10577
914-253-2000

Michael D. White
Chairman and Chief Executive Officer
54. 16 years.

Pepsi-Cola North America
700 Anderson Hill Road
Purchase, NY 10577
914-253-2000

Dawn Hudson
President and Chief Executive Officer
48. 9 years.

QTG (Quaker Tropicana Gatorade)
555 West Monroe Street
Chicago, IL 60661
312-821-1000

John C. Compton
President and Chief Executive Officer
44. 22 years.

Listings include age and years of PepsiCo experience.

PepsiCo Board of Directors

Seated, left to right: Victor J. Dzau, M.D., Sharon Percy Rockefeller, Steven S Reinemund, Franklin A. Thomas, Robert E. Allen.

Standing, left to right: Arthur C. Martinez, Indra K. Nooyi, John F. Akers, Alberto Ibargüen, Ray L. Hunt, Cynthia M. Trudell, Daniel Vasella, James J. Schiro, Dina Dublon.

John F. Akers
Former Chairman of the Board and Chief Executive Officer, International Business Machines
71. Elected 1991.

Robert E. Allen
Former Chairman of the Board and Chief Executive Officer, AT&T Corp.
71. Elected 1990.

Dina Dublon
Consultant, Retired Chief Financial Officer, JPMorgan Chase
52. Elected 2005.

Victor J. Dzau, M.D.
Chancellor for Health Affairs, President & Chief Executive Officer, Duke University Health Systems, Duke University Medical Center
60. Elected 2005.

Ray L. Hunt
Chief Executive Officer, Hunt Oil Company and Chairman, Chief Executive Officer and President, Hunt Consolidated, Inc.
62. Elected 1996.

Alberto Ibargüen
President and Chief Executive Officer, John S. and James L. Knight Foundation
62. Elected 2005.

Arthur C. Martinez
Former Chairman of the Board, President and Chief Executive Officer, Sears, Roebuck and Co.
66. Elected 1999.

Indra K. Nooyi
President and Chief Financial Officer, PepsiCo
50. Elected 2001.

Steven S Reinemund
Chairman of the Board and Chief Executive Officer, PepsiCo
57. Elected 1996.

Sharon Percy Rockefeller
President and Chief Executive Officer, WETA Public Stations
61. Elected 1986.

James J. Schiro
Chief Executive Officer, Zurich Financial Services
60. Elected 2003.

Franklin A. Thomas
Consultant, TFF Study Group
71. Elected 1994.

Cynthia M. Trudell
President, Sea Ray Group
52. Elected 2000.

Daniel Vasella
Chairman of the Board and Chief Executive Officer, Novartis AG
52. Elected 2002.

Listings include age and year elected a PepsiCo director.

Our Ethnic Advisory Boards provide management with external viewpoints on issues related to diversity and inclusion, especially in the marketplace.

Ethnic Advisory Boards

Board membership is established for external individuals based on their diverse backgrounds, experiences and points of view. These boards provide counsel and advice on a range of business areas including:

- Marketing to targeted communities.
- Building alliances with retailers.

Seated, left to right:
Ray M. Robinson,
Benaree Pratt Wiley,
Earl G. Graves, Sr.,
Dawn Hudson,
Keith Clinkscales.

Standing, left to right:
Kweisi Mfume,
Amy Hilliard,
Warren M. Thompson,
Jerri DeVard,
Glenda McNeal,
John Compton,
Johnny F. Johnson,
Roderick D. Gillum,
Darlene Williamson, Ph.D.,
Robert Holland,
Reverend Dr. Franklyn Richardson,
Darwin N. Davis, Sr.,
Clarence Avant,
Reverend Al Sharpton.

African American Advisory Board

Clarence Avant
Chairman, Interior Music
Joined 1999.

Keith Clinkscales
Senior Vice President and General Manager, ESPN Publishing
Joined 1999.

John Compton
President and Chief Executive Officer, QTG
Joined 2005.

Darwin N. Davis, Sr.
Consultant, Retired Senior Vice President, AXA/Equitable
Joined 1999.

Jerri DeVard
Senior Vice President, Brand Management and Marketing Communications, Verizon Communications
Joined 2002.

Roderick D. Gillum
Vice President, Corporate Responsibility and Diversity, General Motors
Joined 2005.

Earl G. Graves, Sr.
Chairman, Earl G. Graves Ltd.
Chairman of the Advisory Board
Joined 1999.

Amy Hilliard
President and Chief Executive Officer, The Hilliard Group & The ComfortCake Co.
Joined 1999.

Robert Holland
Partner, Williams Capital
Joined 1999.

Dawn Hudson
President and Chief Executive Officer, Pepsi-Cola North America
Joined 1999.

Johnny F. Johnson
Chief Executive Officer, KA Management
Joined 1999.

Glenda McNeal
Senior Vice President Global Partnerships, American Express
Joined 1999.

Kweisi Mfume
Former President and Chief Executive Officer, National Association for the Advancement of Colored People (NAACP)
Joined 2005.

Reverend Dr. Franklyn Richardson
Senior Minister, Grace Baptist Church
Joined 1999.

Ray M. Robinson
Chairman, Citizens Trust Bank
Joined 1999.

Reverend Al Sharpton
President, National Action Network
Joined 1999.

Warren M. Thompson
Chairman and Chief Executive Officer, Thompson Hospitality Corporation, Inc.
Joined 2002.

Benaree Pratt Wiley
Retired President and Chief Executive Officer, The Partnership
Joined 2002.

Darlene Williamson, Ph.D.
Former President and Chief Executive Officer, Performax Consulting Services
Joined 1999.

- Creating products for a more diverse consumer base.
- Developing a more diverse supplier base and other business relationships.
- Promoting PepsiCo's diversity and inclusion efforts.
- Recommending diverse talent for employment opportunities.
- Encouraging the expansion of diversity representation among PepsiCo employees.
- Providing a perspective on diversity and inclusion issues or questions.

Our African American Advisory Board was formed in 1999. The Latino/Hispanic Advisory Board was established in 2000.

Some of our businesses outside the United States also are forming similar boards. For example, our Canada business recently convened an Asian Advisory Board.

We welcome Roderick D. Gillum, Kweisi Mfume and John Compton, who moves from the Latino/Hispanic Advisory Board, to the African American Advisory Board. We regret the passing of our esteemed member, Johnnie L. Cochran. To our Latino/ Hispanic Advisory Board, we welcome Maria Contreras-Sweet.

Seated, left to right:
Gilbert Aranza,
Irene Rosenfeld,
Raúl Yzaguirre,
Maria Contreras-Sweet,
Carlos H. Arce, Ph.D.

Standing, left to right:
Victor Arias, Jr.,
Carlos A. Saladrigas,
Deborah Rosado Shaw,
Isabel Valdés,
Ricardo R. Fernández, Ph.D.,
Douglas X. Patiño, Ph.D.,
Raquel Malo.

Latino/Hispanic Advisory Board

Gilbert Aranza
President, Star Concessions
The MultiRestaurant Group
Joined 2000.

Carlos H. Arce, Ph.D.
President and Founder,
NuStats
Joined 2000.

Victor Arias, Jr.
Partner,
Heidrick & Struggles
Joined 2000.

Maria Contreras-Sweet
President,
Fortius Holdings, LLC.
Joined 2005.

Ricardo R. Fernández, Ph.D.
President, Lehman College,
The City University of New York
Joined 2003.

Raquel Malo
Director, High Performance
Nutrition, Human Performance
Institute
Joined 2004.

Douglas X. Patiño, Ph.D.
Vice Chancellor Emeritus and
Professor,
California State University
Joined 2000.

Irene Rosenfeld
Chairman and Chief
Executive Officer,
Frito-Lay North America
Joined 2004.

Carlos A. Saladrigas
Chairman,
Premier American Bank
Joined 2003.

Deborah Rosado Shaw
Chief Executive Officer,
Dream BIG! Enterprises, LLC
Joined 2000.

Isabel Valdés
Consultant, Author,
Public Speaker
Joined 2001.

Raúl Yzaguirre
Presidential Professor,
Center for Community
Development and
Civil Rights,
Arizona State University
Chairman of the Advisory Board
Joined 2000.

Blue Ribbon Health and Wellness Advisory Board

PepsiCo's Blue Ribbon Health and Wellness Advisory Board addresses the growing opportunity in health and wellness.

The Board provides advice and expertise on a variety of health and wellness initiatives including:

- Improving the healthfulness of our existing products.
- Evaluating our efforts to develop new better-for-you and good-for-you products.
- Providing access to resources that promote health and encourage active lifestyles.
- Identifying emerging opportunities in the area of health and wellness.
- Connecting us to thought leaders and policy makers in the area of health and wellness.

Our international businesses are seeking advice in a similar manner. For example, Brazil has created the PepsiCo Panel of Experts, made up of renowned scientists and professionals in the areas of physical activity, cardiology, endocrinology, nutrition and pediatrics.

Front row, left to right: Kristy F. Woods, M.D., M.P.H., Gro Brundtland, M.D., Antonia Demas, Ph.D., David Heber, M.D., Ph.D., Dean Ornish, M.D., Ph.D., Samuel Ward Casscells, III, M.D., Brock Leach, Susan Love, M.D. Second row, left to right: Janet E. Taylor, M.D., James Hill, Ph.D. Back row, left to right: Kenneth Cooper, M.D., M.P.H., Mario Maranhão, M.D., George Graham, Ph.D., Pamela Peeke, M.D., M.P.H., Fernando Trevino, Ph.D., M.P.H., Kenneth Gladish, Ph.D., David Kessler, M.D., J.D., Ambassador Thomas S. Foley, Governor James B. Hunt, Jr.

Gro Brundtland, M.D.
Former Director General, World Health Organization, United Nations, Former Prime Minister, Norway
Joined 2004.

Samuel Ward Casscells, III, M.D.
John Edward Tyson Distinguished Professor of Medicine & Public Health and Vice President for Biotechnology, University of Texas Health & Science Center at Houston
Joined 2003.

Kenneth Cooper, M.D., M.P.H.
President and Founder, The Cooper Aerobics Center
Joined 2003.

Antonia Demas, Ph.D.
Director, Food Studies Institute
Joined 2003.

Ambassador Thomas S. Foley
Partner, Akin, Gump, Strauss, Hauer & Feld, LLP, Former Speaker of the U.S. House of Representatives and Former U.S. Ambassador to Japan
Joined 2003.

Kenneth Gladish, Ph.D.
National Executive Director, YMCA of the USA
Joined 2003.

George Graham, Ph.D.
Chairman, Department of Kinesiology, Pennsylvania State University
Joined 2003.

David Heber, M.D., Ph.D.
Professor of Medicine & Public Health Director, UCLA Center for Human Nutrition
Joined 2003.

James Hill, Ph.D.
Professor of Pediatrics & Medicine, University of Colorado Health Sciences Center, Founder, America On the Move
Joined 2003.

Governor James B. Hunt, Jr.
Attorney, Womble Carlyle Sandridge & Rice, Former Governor of North Carolina
Joined 2003.

David Kessler, M.D., J.D.
Dean, School of Medicine, Vice Chancellor for Medical Affairs, University of California, San Francisco
Joined 2003.

Brock Leach
Retired Senior Vice President, New Growth Platforms and Chief Innovation Officer, PepsiCo
Joined 2003.

Susan Love, M.D.
Professor of Surgery, The David Geffen School of Medicine at UCLA and Founder of Lluminari, multimedia women's health company
Joined 2003.

Mario Maranhão, M.D.
Immediate Past President, World Heart Federation, Professor of Cardiology, Evangelic School of Medicine and Hospital
Joined 2004.

Dean Ornish, M.D.
Founder and Director, Preventive Medicine Research Institute, *Chairman of the Advisory Board*
Joined 2003.

Pamela Peeke, M.D., M.P.H.
Assistant Professor, University of Maryland School of Medicine, Expert and speaker in nutrition, stress and integrative medicine
Joined 2003.

Janet E. Taylor, M.D.
Clinical Instructor, Pediatric Psychiatry, Harlem Hospital, President/CEO, Mind Projects, Inc., Lluminari Expert Network
Joined 2004.

Fernando Trevino, Ph.D., M.P.H.
Dean, School of Public Health, University of North Texas, Past President, World Federation of Public Health Associations, Former Executive Director, American Public Health Association
Joined 2004.

Kristy F. Woods, M.D., M.P.H.
Professor of Medicine and Director, Maya Angelou Research Center on Minority Health, Wake Forest University School of Medicine, Maya Angelou Research Center on Minority Health
Joined 2005.

Management's Discussion and Analysis and Consolidated Financial Statements

Our Business

Our Critical Accounting Policies

Our Financial Results

Notes to Consolidated Financial Statements

Our Business

Our discussion and analysis is an integral part of understanding our financial results. Definitions of key terms can be found in the glossary on page 76. Tabular dollars are presented in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless noted, and are based on unrounded amounts. Percentage changes are based on unrounded amounts.

Our Operations

We are a leading, global snack and beverage company. We manufacture, market and sell a variety of salty, convenient, sweet and grain-based snacks, carbonated and non-carbonated beverages and foods. We are organized into four divisions:

- Frito-Lay North America,
- PepsiCo Beverages North America,
- PepsiCo International, and
- Quaker Foods North America.

Our North American divisions operate in the United States and Canada. Our international divisions operate in over 200 countries, with our largest operations in Mexico and the United Kingdom. Additional information concerning our divisions and geographic areas is presented in Note 1.

Frito-Lay North America

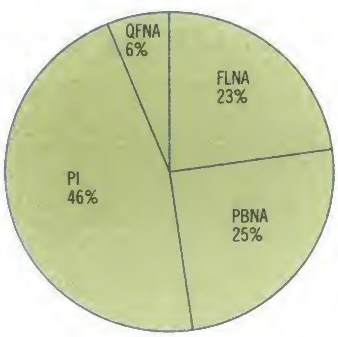
Frito-Lay North America (FLNA) manufactures or uses contract manufacturers, markets, sells and distributes branded snacks. These snacks include Lay's potato chips, Doritos tortilla chips, Cheetos cheese flavored snacks, Tostitos tortilla chips, Fritos corn chips, branded dips, Ruffles potato chips, Quaker Chewy granola bars, Rold Gold pretzels, Sun Chips multigrain snacks, Munchies snack mix, Grandma's cookies, Lay's Stax potato crisps, Quaker Quakes corn and rice snacks, Quaker Fruit & Oatmeal bars, Cracker Jack candy coated popcorn and Go Snacks. FLNA branded products are sold to independent distributors and retailers.

All of our divisions positively contributed to net revenue and operating profit growth in 2005.

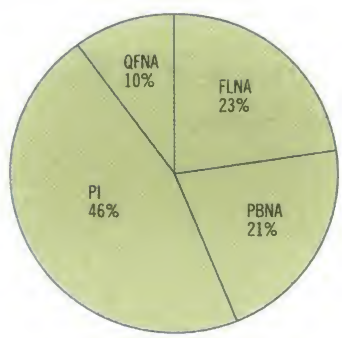
PepsiCo Beverages North America

PepsiCo Beverages North America (PBNA) manufactures or uses contract manufacturers, markets and sells beverage concentrates, fountain syrups and finished goods, under various beverage brands including Pepsi, Mountain Dew, Gatorade, Tropicana Pure Premium, Sierra Mist, Tropicana juice drinks, Mug, Propel, SoBe, Tropicana Twister, Dole and Slice. PBNA also manufactures, markets and sells ready-to-drink tea and coffee products through joint ventures with Lipton and Starbucks. In addition, PBNA licenses the Aquafina water brand to its bottlers and markets this brand. PBNA sells concentrate and finished goods for some of these brands to bottlers licensed by us, and some of these branded products are sold directly by us to independent distributors and retailers. The franchise bottlers sell our brands as finished goods to independent distributors and retailers. PBNA's volume reflects sales to its independent distributors and retailers, and the sales of beverages bearing our trademarks that franchise bottlers have reported as sold to independent distributors and retailers.

Net Revenue Contribution to Growth



Operating Profit Contribution to Growth



PepsiCo International

PepsiCo International (PI) manufactures through consolidated businesses as well as through noncontrolled affiliates, a number of leading salty and sweet snack brands including Gamesa and Sabritas in Mexico, Walkers in the United Kingdom, and Smith's in Australia. Further, PI manufactures or uses contract manufacturers, markets and sells many Quaker brand snacks. PI also manufactures, markets and sells beverage concentrates, fountain syrups and finished goods under the brands Pepsi, 7UP, Mirinda, Gatorade, Mountain Dew and Tropicana. These brands are sold to franchise bottlers, independent distributors and retailers. However, in certain markets, PI operates its own bottling plants and distribution facilities. PI also licenses the Aquafina water brand to certain of its franchise bottlers. PI reports two measures of volume. Snack volume is reported on a system-wide basis, which includes our own volume and the volume sold by our noncontrolled affiliates. Beverage volume reflects company-owned and franchise bottler sales of beverages bearing our trademarks to independent distributors and retailers.

Quaker Foods North America

Quaker Foods North America (QFNA) manufactures or uses contract manufacturers, markets and sells cereals, rice, pasta and other branded products. QFNA's products include Quaker oatmeal, Aunt Jemima mixes and syrups, Quaker grits, Cap'n Crunch and Life ready-to-eat cereals, Rice-A-Roni, Pasta Roni and Near East side dishes. These branded products are sold to independent distributors and retailers.

Our Customers

Our customers include franchise bottlers and independent distributors and retailers. We normally grant our bottlers exclusive contracts to sell and manufacture certain beverage products bearing our trademarks within a specific geographic area. These arrangements specify the amount to be paid by our bottlers for concentrate and full goods and for Aquafina royalties, as well as the manufacturing process required for product quality.

Since we do not sell directly to the consumer, we rely on and provide financial incentives to our customers to assist in the distribution and promotion of our products. For our independent distributors and retailers, these incentives include volume-based rebates, product placement fees, promotions and displays. For our bottlers, these incentives are referred to as bottler funding and are negotiated annually with each bottler to support a variety of trade and consumer programs, such as consumer incentives, advertising support, new product support, and vending and cooler equipment placement. Consumer incentives include coupons, pricing discounts and promotions, such as sweepstakes and other promotional offers. Advertising support is directed at advertising programs and supporting bottler media. New product support includes targeted consumer and retailer incentives and direct marketplace support, such as point-of-purchase materials, product placement fees, media and advertising. Vending and cooler equipment placement programs support the acquisition and placement of vending machines and cooler equipment. The nature and type of programs vary annually. The level of bottler funding is at our discretion because these incentives are not required by the terms of our bottling contracts.

Retail consolidation has increased the importance of major customers and further consolidation is expected. Sales to Wal-Mart Stores, Inc. represent approximately 9% of our total worldwide net revenue; and our top five retail customers currently represent approximately 26% of our 2005 North American net revenue, with Wal-Mart representing approximately 11%. These percentages include concentrate sales to our bottlers which are used in finished goods sold by them to these retailers. In addition, sales to The Pepsi Bottling Group (PBG) represent approximately 10% of our total net revenue. See "Our Related Party Bottlers" and Note 8 for more information on our anchor bottlers.

Our customers include franchise bottlers and independent distributors and retailers.

Our Related Party Bottlers

We have ownership interests in certain of our bottlers. Our ownership is less than 50% and since we do not control these bottlers, we do not consolidate their results. We include our share of their net income based on our percentage of economic ownership in our income statement as bottling equity income. We have designated three related party bottlers, PBG, PepsiAmericas, Inc. (PAS) and Pepsi Bottling Ventures LLC (PBV), as our anchor bottlers. Our anchor bottlers distribute approximately 62% of our North American beverage volume and approximately 19% of our international beverage volume. Our anchor bottlers participate in the bottler funding programs described above. Approximately 8% of our total 2005 sales incentives are related to these bottlers. See Note 8 for additional information on these related parties and related party commitments and guarantees.

Our Distribution Network

Our products are brought to market through direct-store-delivery, broker-warehouse and foodservice and vending distribution networks. The distribution system used depends on customer needs, product characteristics and local trade practices.

Direct-Store-Delivery

We and our bottlers operate direct-store-delivery systems that deliver snacks and beverages directly to retail stores where the products are merchandised by our employees or our bottlers. Direct-store-delivery enables us to merchandise with maximum visibility and appeal. Direct-store-delivery is especially well-suited to products that are restocked often and respond to in-store promotion and merchandising.

Broker-Warehouse

Some of our products are delivered from our manufacturing plants and warehouses to customer warehouses and retail stores. These less costly systems generally work best for products that are less fragile and perishable, have lower turnover, and are less likely to be impulse purchases.

Direct-store-delivery enables us to merchandise with maximum visibility and appeal.

Foodservice and Vending

Our foodservice and vending sales force distributes snacks, foods and beverages to third-party foodservice and vending distributors and operators, and for certain beverages, distributes through our bottlers. This distribution system supplies our products to schools, businesses, stadiums, restaurants and similar locations.

Our Competition

Our businesses operate in highly competitive markets. We compete against global, regional, local and private label manufacturers on the basis of price, quality, product variety and effective distribution. In measured channels, our chief beverage competitor, The Coca-Cola Company, has a slightly larger share of carbonated soft drink (CSD) consumption in the U.S., while we have a larger share of chilled juices and isotonics. In addition, The Coca-Cola Company maintains a significant CSD share advantage in many markets outside North America. Further, our snack brands hold significant leadership positions in the snack industry worldwide. Our snack brands face local and regional competitors, as well as national and global snack competitors, and compete on issues related to price, quality, variety and distribution.

Success in this competitive environment is dependent on effective promotion of existing products and the introduction of new products. We believe that the strength of our brands, innovation and marketing, coupled with the quality of our products and flexibility of our distribution network, allow us to compete effectively.

Other Relationships

Certain members of our Board of Directors also serve on the boards of certain vendors and customers. Those Board members do not participate in our vendor selection and negotiations nor in our customer negotiations. Our transactions with these vendors and customers are in the normal course of business and are consistent with terms negotiated with other vendors and customers. In addition, certain of our employees serve on the boards of our anchor bottlers and other affiliated companies and do not receive incremental compensation for their Board services.

Our Business Risks

We are subject to risks in the normal course of business due to adverse developments with respect to:

- **product demand,**
- **our reputation,**
- **information technology,**
- **supply chain,**
- **retail consolidation and the loss of major customers,**
- **global economic and environmental conditions,**
- **the regulatory environment,**
- **workforce retention,**
- **raw materials and energy,**
- **competition, and**
- **market risks.**

Demand for our products may be adversely affected by changes in consumer preferences and tastes.

We are a consumer products company operating in highly competitive markets and rely on continued demand for our products. To generate revenues and profits, we must sell products that appeal to our customers and to consumers. Any significant changes in consumer preferences and our inability to anticipate and react to such changes could result in reduced demand for our products and erosion of our competitive and financial position. Our success depends on our ability to respond to consumer trends, such as consumer health concerns about obesity, product attributes and ingredients. In addition, changes in product category consumption and consumer demographics could result in reduced demand for our products. Consumer preferences may shift due to a variety of factors, including the aging of the general population, changes in social trends, changes in travel, vacation or leisure activity patterns or a downturn in economic conditions, which may reduce consumers' willingness to purchase premium branded products. Our continued success is also dependent on our product innovation, including maintaining a robust pipeline of new products, and the effectiveness of our advertising campaigns and marketing programs. There can be no assurance as to our continued ability to develop and launch successful new products or variants of existing products, or to effectively execute advertising campaigns and marketing programs. In addition, both the launch and ongoing success of new products and advertising campaigns are inherently uncertain, especially as to their appeal to consumers.

Our success depends on our ability to respond to consumer trends, such as consumer health concerns about obesity, product attributes and ingredients.

Any damage to our reputation could have an adverse effect on our business, financial condition and results of operations.

Maintaining a good reputation globally is critical to selling our branded products. If we fail to maintain high standards for product quality, safety and integrity, our reputation could be jeopardized. Adverse publicity about these types of concerns, whether or not valid, may reduce demand for our products or cause production and delivery disruptions. If any of our products becomes unfit for consumption, misbranded or causes injury, we may have to engage in a product recall and/or be subject to liability. A widespread product recall or a significant product liability judgment could cause our products to be unavailable for a period of time, which could further reduce consumer demand and brand equity. Failure to maintain high ethical, social and environmental standards for all of our operations and activities could also jeopardize our reputation. Damage to our reputation or loss of consumer confidence in our products for any of these reasons could have a material adverse effect on our business, financial condition and results of operations, as well as require additional resources to rebuild our reputation.

Maintaining a good reputation globally is critical to selling our branded products.

If we are not able to build and sustain proper information technology infrastructure, our business could suffer.

We depend on information technology as an enabler to operating efficiently and interfacing with customers, as well as maintaining financial accuracy and efficiency. If we do not allocate, and effectively manage, the resources necessary to build and sustain the proper technology infrastructure, we could be subject to transaction errors, processing inefficiencies, the loss of customers, business disruptions, or the loss of or damage to intellectual property through security breach.

We have embarked on a multiyear Business Process Transformation (BPT) initiative that includes the delivery of an SAP enterprise resource planning application, as well as the migration to common business processes across our North American operations. There can be no certainty that

these programs will deliver the expected benefits. The failure to deliver our goals may impact our ability to (1) process transactions accurately and efficiently and (2) remain in step with the changing needs of the trade, which could result in the loss of customers. In addition, the failure to either deliver the application on time, or anticipate the necessary readiness and training needs, could lead to business disruption.

Our ability to make, move and sell products is critical to our success.

As with all large systems, our information systems could be penetrated by outside parties intent on extracting information, corrupting information or disrupting business processes. Such unauthorized access could disrupt our business and could result in the loss of assets.

Disruption of our supply chain could have an adverse effect on our business, financial condition and results of operations.

Our ability to make, move and sell products is critical to our success. Damage or disruption to our manufacturing or distribution capabilities due to weather, natural disaster, fire or explosion, terrorism, pandemic, strikes or other reasons could impair our ability to manufacture or sell our products. Failure to take adequate steps to mitigate the likelihood or potential impact of such events, or to effectively manage such events if they occur, could adversely affect our business, financial condition and results of operations, as well as require additional resources to restore our supply chain.

Trade consolidation or the loss of any key customer could adversely affect our financial performance.

There is a greater concentration of our customer base around the world generally due to the continued consolidation of retail trade. As retail ownership becomes more concentrated, retailers demand lower pricing and increased promotional programs. Further, as larger retailers increase utilization of their own distribution networks and private label brands, the competitive advantages we derive from our go-to-market systems and brand equity may be eroded. Failure to appropriately respond to these trends or to offer effective sales incentives and marketing programs to our customers could reduce our ability to secure adequate shelf space at our retailers and adversely affect our financial performance.

We must maintain mutually beneficial relationships with our key customers, including our retailers and anchor bottlers, to effectively compete. Loss of any of our key customers could have an adverse effect on our business, financial condition and results of operations. See "Our Customers," "Our Related Party Bottlers" and Note 8 to our consolidated financial statements for more information on our customers, including our anchor bottlers.

Our business may be adversely impacted by unfavorable economic or environmental conditions or political or other developments and risks in the countries in which we operate.

Unfavorable global economic or environmental changes, political conditions or other developments may result in business disruption, supply constraints, foreign currency devaluation, inflation, deflation or decreased demand. Economic conditions in North America could also adversely impact growth. For example, rising fuel costs may impact the sales of our products in convenience stores where our products are generally sold in higher margin single serve packages. Our international operations accounted for over a third of our evenue for the period ended December 31, 2005. Unstable economic and political conditions or civil unrest in the countries in which we operate could have adverse impacts on our business results or financial condition.

Regulatory decisions and changes in the legal and regulatory environment could increase our costs and liabilities or limit our business activities.

The conduct of our businesses, and the production, distribution, sale, advertising, labeling, safety, transportation and use of many of our products, are subject to various laws and regulations administered by federal, state and local governmental agencies in the United States, as well as to foreign laws and regulations administered by government entities and agencies in markets in which we operate. In many jurisdictions, compliance with competition laws is of special importance to us due to our competitive position in those jurisdictions. These laws and regulations may change, sometimes dramatically, as a result of political, economic or social events. Changes in laws, regulations or governmental policy and the related interpretations may alter the environment in which we do business and, therefore, may impact our results or increase our costs or liabilities. Such regulatory environment changes include changes in food and drug laws, laws related to advertising and deceptive marketing practices, accounting standards, taxation requirements, competition laws and environmental laws, including California Proposition 65 and the regulation of water consumption and treatment. In particular, governmental bodies in countries where we operate may impose new labeling, product or production requirements, or other restrictions. Regulatory authorities under whose laws we operate may also have enforcement powers that can subject us to actions such as product recall, seizure of products or other sanctions, which could have an adverse effect on our sales or damage our reputation. See also "Regulatory Environment and Environmental Compliance."

Changes in laws, regulations or governmental policy may alter the environment in which we do business.

If we are unable to hire or retain key employees, it could have a negative impact on our business.

Our continued growth requires us to develop our leadership bench and to implement programs, such as our long-term incentive program, designed to retain talent. However, there is no assurance that we will continue to be able to hire or retain key employees. We compete to hire new employees, and then must train them and develop their skills and competencies. Our

operating results could be adversely affected by increased costs due to increased competition for employees, higher employee turnover or increased employee benefit costs. Any unplanned turnover could deplete our institutional knowledge base and erode our competitive advantage.

Our operating results may be adversely affected by increased costs or shortages of raw materials.

We are exposed to the market risks arising from adverse changes in commodity prices, affecting the cost of our raw materials and energy. The raw materials and energy which we use for the production of our products are largely commodities that are subject to price volatility and fluctuations in availability caused by changes in global supply and demand, weather conditions, agricultural uncertainty or governmental controls. We purchase these materials and energy mainly in the open market. If commodity price changes result in unexpected increases in raw materials and energy costs, we may not be able to increase our prices to offset these increased costs without suffering reduced volume, revenue and operating income.

Our business could suffer if we are unable to compete effectively.

Our businesses operate in highly competitive markets. We compete against global, regional and private label manufacturers on the basis of price, quality, product variety and effective distribution. Increased competition and anticipated actions by our competitors could lead to downward pressure on prices and/or a decline in our market share, either of which could adversely affect our results. See "Our Competition" for more information about our competitors.

Market Risks

We are exposed to the market risks arising from adverse changes in:

- **commodity prices, affecting the cost of our raw materials and energy,**
- **foreign exchange rates,**
- **interest rates,**
- **stock prices, and**
- **discount rates affecting the measurement of our pension and retiree medical liabilities.**

In the normal course of business, we manage these risks through a variety of strategies, including productivity initiatives, global purchasing programs and hedging strategies. Ongoing productivity initiatives involve the identification and effective implementation of meaningful cost saving opportunities or efficiencies. Our global purchasing programs include fixed-price purchase orders and pricing agreements. Our hedging strategies involve the use of derivatives. Certain derivatives are designated as either cash flow or fair value hedges and qualify for hedge accounting treatment, while others do not qualify and are marked to market through earnings. We do not use derivative instruments for trading or speculative purposes and we limit our exposure to individual counterparties to manage credit risk. The fair value of our derivatives fluctuates based on market rates and prices. The sensitivity of our derivatives to these market fluctuations is discussed below. See Note 10 for further discussion of these derivatives and our hedging policies. See "Our Critical Accounting Policies" for a discussion of the exposure of our pension plan assets and pension and retiree medical liabilities to risks related to stock prices and discount rates.

We do not use derivative instruments for trading or speculative purposes.

Inflationary, deflationary and recessionary conditions impacting these market risks also impact the demand for and pricing of our products.

Commodity Prices

Our open commodity derivative contracts had a face value of $89 million at December 31, 2005 and $155 million at December 25, 2004. The open derivative contracts designated as accounting hedges resulted in net unrecognized gains of $39 million at December 31, 2005 and an unrecognized loss of $1 million at December 25, 2004. We estimate that a 10% decline in commodity prices would have reduced our unrecognized gains on open contracts to $35 million in 2005 and increased our unrecognized losses to $9 million in 2004. The open derivatives contracts that were not designated as accounting hedges resulted in net recognized losses of $3 million in 2005 and $2 million in 2004.

We estimate that a 10% decline in commodity prices would have increased our recognized losses on open contracts to $4 million in 2005 and to $5 million in 2004.

In 2006, we expect continued pricing pressures on our raw materials and energy costs. We expect to be able to mitigate the impact of these increased costs through our hedging strategies and ongoing productivity initiatives.

Foreign Exchange

Financial statements of foreign subsidiaries are translated into U.S. dollars using period-end exchange rates for assets and liabilities and weighted-average exchange rates for revenues and expenses. Adjustments resulting from translating net assets are reported as a separate component of accumulated other comprehensive loss within shareholders' equity under the caption currency translation adjustment.

Our operations outside of the U.S. generate over a third of our net revenue of which Mexico, the United Kingdom and Canada comprise nearly 20%. As a result, we are exposed to foreign currency risks, including unforeseen economic changes and political unrest. During 2005, net favorable foreign currency, primarily increases in the Mexican peso, Brazilian real, and Canadian dollar, contributed over 1 percentage point to net revenue growth. Currency declines which are not offset could adversely impact our future results.

Exchange rate gains or losses related to foreign currency transactions are recognized as transaction gains or losses in the income statement as incurred. We may enter into derivatives to manage our exposure to foreign currency transaction risk. Our foreign currency derivatives had a total face value of $1.1 billion at December 31, 2005 and $908 million at December 25, 2004. The contracts designated as accounting hedges resulted in net unrecognized losses of $9 million at December 31, 2005 and $27 million at December 25, 2004. We estimate that an unfavorable 10% change in the exchange rates would have resulted in unrecognized losses of $81 million in 2005 and $110 million in 2004. The contracts not designated as accounting hedges resulted in net recognized gains of $14 million and less than $1 million at December 31, 2005 and December 25, 2004, respectively. These gains were almost entirely offset by changes in the underlying hedged items, resulting in no net impact on earnings.

Interest Rates

We centrally manage our debt and investment portfolios considering investment opportunities and risks, tax consequences and overall financing strategies. We may use interest rate and cross currency interest rate swaps to manage our overall interest expense and foreign exchange risk. These instruments effectively change the interest rate and currency of specific debt issuances. These swaps are entered into concurrently with the issuance of the debt that they are intended to modify. The notional amount, interest payment and maturity date of the swaps match the principal, interest payment and maturity date of the related debt. Our counterparty credit risk is considered low because these swaps are entered into only with strong creditworthy counterparties, are generally settled on a net basis and are of relatively short duration.

Assuming year-end 2005 and 2004 variable rate debt and investment levels, a one point increase in interest rates would have decreased net interest expense by $8 million in 2005 and $11 million in 2004.

Stock Prices

A portion of our deferred compensation liability is tied to certain market indices and our stock price. We manage these market risks with mutual fund investments and prepaid forward contracts for the purchase of our stock. The combined gains or losses on these investments are substantially offset by changes in our deferred compensation liability.

Our Approach to Managing Risks

The achievement of our strategic and operating objectives will necessarily involve taking risks. Our risk management process is intended to ensure that risks are taken knowingly and purposefully. As such, we leverage an integrated risk management framework to identify, assess, prioritize, manage, monitor, and communicate risks across the company. This framework includes:

In 2005, we continued our effort to drive risk mitigation focus to where risks can be most efficiently and effectively managed.

- the PepsiCo Executive Risk Council (PERC), comprised of a cross-functional, geographically diverse, senior management group which identifies, assesses, prioritizes and addresses primarily strategic and reputational risks;
- Division Risk Committees (DRCs), comprised of cross-functional senior management teams which meet regularly each year to identify, assess, prioritize and address division-specific operating risks;
- PepsiCo's Risk Management Office, which manages the overall process, provides ongoing guidance, tools and analytical support to the PERC and the DRCs, identifies and assesses potential risks, and facilitates ongoing communication between the parties, as well as to PepsiCo's Audit Committee; and
- PepsiCo Corporate Audit, which confirms the ongoing effectiveness of the risk management framework through periodic audit and review procedures.

In 2005, we continued our effort to drive risk mitigation focus to where risks can be most efficiently and effectively managed and reinforced ownership and accountability for risk management within the business. Some highlights include:

- With respect to product demand, we continued to focus on the development of products that respond to consumer trends, such as comsumer health concerns about obesity, product attributes and ingredients, including reformulating products to lower sugar, fats, and sodium; adding ingredients that deliver health benefits; and expanding our offering of portion-controlled packages. Smart Spot eligible products continued to be the fastest growing part of our North American product portfolio. We continued to focus on marketing our products in ways that promote healthier lifestyles. We helped create and endorsed the American Beverage Association's new schools policy, which defines the types of products that may be sold in schools. We actively promoted healthy energy balance through our national sponsorship of America On the Move, a program designed to help families take simple steps to maintain a healthy energy balance.
- We enhanced the coordination of our Division-led product integrity efforts through the creation of the PepsiCo Product Integrity Council (PPIC), a cross-functional forum to share leading practices and confer about areas of potential risk.

Smart Spot eligible products continued to be the fastest growing part of our North American product portfolio.

- We continued to enhance our internal IT infrastructure, by consolidating and updating technology and retiring older technology, as well as improving our information security capabilities.
- We continued implementation of our BPT initiative, which we believe will enable us to remain in step with the changing needs of our customers. Overall BPT project governance is provided through steering committees headed by senior executives and a team is in place to drive effective risk management and quality processes and to build an internal control environment compliant with the Sarbanes-Oxley Act.
- We continue to assess our capability to mitigate potential business disruptions and evaluate an integrated approach to business disruption management, including disaster recovery, crisis management, and business continuity.
- We established a compliance and ethics leadership structure, appointing an SVP, Deputy General Counsel who is focusing on business practices and compliance, prioritizing projects to enhance the effectiveness of our compliance and ethics program, including developing a multilingual Code of Conduct training program that will be rolled out in 2006.

We established a compliance and ethics leadership structure in 2005.

- We have implemented human resource programs which focus on diversity and inclusion, leadership development, succession planning, and employee work-life flexibility, and are aimed at hiring, developing, and retaining our talented and motivated workforce.

Forward-Looking and Cautionary Statements

We discuss expectations regarding our future performance, such as our business outlook, in our annual and quarterly reports, press releases, and other written and oral statements. These "forward-looking statements" are based on currently available competitive, financial and economic data and our operating plans. They are inherently uncertain, and investors must recognize that events could turn out to be significantly different from our expectations. We undertake no obligation to update any forward-looking statement. The above discussion of risks is by no means all inclusive but is designed to highlight what we believe are important factors to consider when evaluating our trends and future results.

Our Critical Accounting Policies

An appreciation of our critical accounting policies is necessary to understand our financial results. These policies may require management to make difficult and subjective judgments regarding uncertainties, and as a result, such estimates may significantly impact our financial results. The precision of these estimates and the likelihood of future changes depend on a number of underlying variables and a range of possible outcomes. Other than our accounting for stock-based compensation and pension plans, our critical accounting policies do not involve the choice between alternative methods of accounting. We applied our critical accounting policies and estimation methods consistently in all material respects, and for all periods presented, and have discussed these policies with our Audit Committee.

Our critical accounting policies arise in conjunction with the following:

- revenue recognition,
- brand and goodwill valuations,
- income tax expense and accruals,
- stock-based compensation expense, and
- pension and retiree medical plans.

In connection with our ongoing BPT initiative, we aligned certain accounting policies across our divisions in 2005. We conformed our methodology for calculating our bad debt reserves and modified our policy for recognizing revenue for products shipped to customers by third-party carriers. Additionally, we conformed our method of accounting for certain costs, primarily warehouse and freight. These changes reduced our net revenue by $36 million and our operating profit by $60 million in 2005. We also made certain reclassifications on our Consolidated Statement of Income in the fourth quarter of 2005 from cost of sales to selling, general and administrative expenses in connection with our BPT initiative. These reclassifications resulted in reductions to cost of sales of $556 million through the third quarter of 2005, $732 million in the full year 2004 and $688 million in the full year 2003, with corresponding increases to selling, general and administrative expenses in those periods. These reclassifications had no net impact on operating profit and have been made to all periods presented for comparability.

There have been no new accounting pronouncements issued or effective during 2005 that have had, or are expected to have, a material impact on our consolidated financial statements.

Revenue Recognition

Our products are sold for cash or on credit terms. Our credit terms, which are established in accordance with local and industry practices, typically require payment within 30 days of delivery in the U.S. and may allow discounts for early payment. We recognize revenue upon shipment or delivery to our customers based on written sales terms that do not allow for a right of return. However, our policy for DSD and chilled products is to remove and replace damaged and out-of-date products from store shelves to ensure that consumers receive the product quality and freshness they expect. Similarly, our policy for warehouse distributed products is to replace damaged and out-of-date products. Based on our historical experience with this practice, we have reserved for anticipated damaged and out-of-date products. Our bottlers have a similar replacement policy and are responsible for the products they distribute.

Our policy is to provide customers with product when needed. In fact, our commitment to freshness and product dating serves to regulate the quantity of product shipped or delivered. In addition, DSD products are placed on the shelf by our employees with customer shelf space limiting the quantity of product. For product delivered through our other distribution networks, customer inventory levels are monitored.

As discussed in "Our Customers," we offer sales incentives and discounts through various programs to customers and consumers. Sales incentives and discounts are accounted for as a reduction of sales and totaled $8.9 billion in 2005, $7.8 billion in 2004 and $7.1 billion in 2003. Sales incentives include payments to customers for performing merchandising activities on our behalf, such as payments for in-store displays, payments to gain distribution of new products, payments for shelf space and discounts to promote lower retail prices. A number of our sales incentives, such as bottler funding and customer volume rebates, are based on annual targets, and accruals are established during the year for the expected payout. These accruals are based on contract terms and our historical experience with similar programs and require management judgment with respect to estimating customer participation and performance levels. Differences between estimated expense and actual incentive costs are normally insignificant and are recognized in earnings in the

period such differences are determined. The terms of most of our incentive arrangements do not exceed a year, and therefore do not require highly uncertain long-term estimates. For interim reporting, we estimate total annual sales incentives for most of our programs and record a pro rata share in proportion to revenue. Certain arrangements extend beyond one year. For example, fountain pouring rights may extend up to 15 years. The costs incurred to obtain these arrangements are recognized over the contract period as a reduction of revenue, and the remaining balances of $321 million at year-end 2005 and $337 million at year-end 2004 are included in current assets and other assets in our Consolidated Balance Sheet.

Differences between estimated expense and actual incentive costs are normally insignificant and are recognized in earnings in the period such differences are determined.

We estimate and reserve for our bad debt exposure based on our experience with past due accounts. In 2005, our method of determining the reserves was conformed across our divisions in connection with our BPT initiative, as discussed above. Bad debt expense is classified within selling, general and administrative expenses in our Consolidated Statement of Income.

Brand and Goodwill Valuations

We sell products under a number of brand names, many of which were developed by us. The brand development costs are expensed as incurred. We also purchase brands and goodwill in acquisitions. Upon acquisition, the purchase price is first allocated to identifiable assets and liabilities, including brands, based on estimated fair value, with any remaining purchase price recorded as goodwill.

We believe that a brand has an indefinite life if it has significant market share in a stable macroeconomic environment and a history of strong revenue and cash flow performance that we expect to continue for the foreseeable future. If these perpetual brand criteria are not met, brands are amortized over their expected useful lives, which generally range from five to 40 years. Determining the expected life of a brand requires considerable management judgment and is based on an evaluation of a number of factors, including the competitive environment, market share, brand history and the macroeconomic environment of the countries in which the brand is sold.

Goodwill, including the goodwill that is part of our noncontrolled bottling investment balances, and perpetual brands are not amortized. Perpetual brands and goodwill are assessed for impairment at least annually to ensure that discounted future cash flows continue to exceed the related book value. A perpetual brand is impaired if its book value exceeds its fair value. Goodwill is evaluated for impairment if the book value of its reporting unit exceeds its fair value. A reporting unit can be a division or business within a division. If the fair value of an evaluated asset is less than its book value, the asset is written down to fair value based on its discounted future cash flows.

Amortizable brands are only evaluated for impairment upon a significant change in the operating or macroeconomic environment. If an evaluation of the undiscounted cash flows indicates impairment, the asset is written down to its estimated fair value, which is based on its discounted future cash flows.

Considerable management judgment is necessary to evaluate the impact of operating and macroeconomic changes and to estimate future cash flows. Assumptions used in our impairment evaluations, such as forecasted growth rates and our cost of capital, are consistent with our internal forecasts and operating plans. These assumptions could be adversely impacted by certain of the risks discussed in "Our Business Risks."

We did not recognize any impairment charges for perpetual brands or goodwill in the years presented. As of December 31, 2005, we had $5.2 billion of perpetual brands and goodwill, of which 70% related to Tropicana and Walkers.

We did not recognize any impairment charges for perpetual brands or goodwill in the years presented.

Income Tax Expense and Accruals

Our annual tax rate is based on our income, statutory tax rates and tax planning opportunities available to us in the various jurisdictions in which we operate. Significant judgment is required in determining our annual tax rate and in evaluating our tax positions. We establish reserves when, despite our belief that our tax return positions are fully supportable, we believe that certain positions are subject to challenge and that we may not succeed. We adjust these reserves, as well as the related interest, in light of changing facts and circumstances, such as the progress of a tax audit. See Note 5 for additional information regarding our tax reserves.

An estimated effective tax rate for a year is applied to our quarterly operating results. In the event there is a significant or unusual item recognized in our quarterly operating results, the tax attributable to that item is separately calculated and recorded at the same time as that item. We consider the tax benefits from the resolution of prior year tax matters to be such items.

Tax law requires items to be included in our tax returns at different times than the items are reflected in our financial statements. As a result, our annual tax rate reflected in our financial statements is different than that reported in our tax returns (our cash tax rate). Some of these differences are permanent, such as expenses that are not deductible in our tax return, and some differences reverse over time, such as depreciation expense. These temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction or credit in our tax returns in future years for which we have already recorded the tax benefit in our income statement. We establish valuation allowances for our deferred tax assets when we believe expected future taxable income is not likely to support the use of a deduction or credit in that tax jurisdiction. Deferred tax liabilities generally represent tax expense recognized in our financial statements for which payment has been deferred, or expense for which we have already taken a deduction in our tax return but we have not yet recognized as expense in our financial statements.

We repatriated approximately $7.5 billion in earnings previously considered indefinitely reinvested outside the U.S. in the fourth quarter of 2005 in connection with the AJCA.

The American Jobs Creation Act of 2004 (AJCA) created a one-time incentive for U.S. corporations to repatriate undistributed international earnings by providing an 85% dividends received deduction. As approved by our Board of Directors in July 2005, we repatriated approximately $7.5 billion in earnings previously considered indefinitely reinvested outside the U.S. in the fourth quarter of 2005. In 2005, we recorded income tax expense of $460 million associated with this repatriation. Other than the earnings repatriated, we intend to continue to reinvest earnings outside the U.S. for the foreseeable future and therefore have not recognized any U.S. tax expense on these earnings. At December 31, 2005, we had approximately $7.5 billion of undistributed international earnings.

In 2005, our annual tax rate for continuing operations was 36.1% compared to 24.7% in 2004 as discussed in "Other Consolidated Results." The tax rate in 2005 increased 11.4 percentage points primarily as a result of the AJCA tax charge and the absence of the 2004 tax benefits related to the favorable resolution of certain open tax items. For 2006, our annual tax rate is expected to be 28.0%, primarily reflecting the absence of the AJCA tax charge and changes in our concentrate sourcing around the world.

Stock-Based Compensation Expense

We believe that we will achieve our best results if our employees act and are rewarded as business owners. Therefore, we believe stock ownership and stock-based incentive awards are the best way to align the interests of employees with those of our shareholders. Historically, following competitive market practices, we have used stock option grants as our primary form of long-term incentive compensation. These grants are made at the current stock price, meaning each employee's exercise price is equivalent to our stock price on the date of grant. Employees must generally provide three additional years of service to earn the grant, referred to as the vesting period. Our options generally have a 10-year term, which means our employees would have up to seven years after the vesting period to elect to pay the exercise price to purchase one share of our stock for each option exercised. Employees benefit from stock options to the extent our stock price appreciates above the exercise price after vesting and during the term of the grant. There have been no reductions to the exercise price of previously issued awards, and any repricing of awards would require approval of our shareholders.

We believe that we will achieve our best results if our employees act and are rewarded as business owners.

Our new executive compensation program, which became effective in 2004, strengthens the relationship between pay and individual performance through greater differentiation in the amount of base pay, bonus and stock-based compensation based on an employee's job level and performance. The new program results in a shift of both cash and stock-based compensation to our top performing executives. In addition, our new program provides executives, who are awarded long-term incentives based on their performance, with a choice of stock options or restricted stock units (RSUs). RSU expense is based on the fair value of PepsiCo stock on the date of grant and is amortized over the vesting period, generally three years. Each restricted stock unit can be settled in a

share of our stock after the vesting period. Executives who elect RSUs receive one RSU for every four stock options that would have otherwise been granted. Senior officers do not have a choice and are granted 50% stock options and 50% RSUs. Vesting of RSU awards for senior officers is contingent upon the achievement of pre-established performance targets.

We also continued, as we have since 1989, to grant an annual award of stock options to all eligible employees, based on job level or classification under our broad-based stock option program, SharePower. As part of the new compensation program which began in 2004, the SharePower program grant was reduced by approximately 50% for employees in the U.S. and replaced with matching contributions of PepsiCo stock to our 401(k) savings plans. We did not reduce the SharePower award for international employees and continued using tenure, in addition to job level and classification, as a basis for the award. For additional information on our 401(k) savings plans, see Note 7.

Method of Accounting

We account for our employee stock options under the fair value method of accounting using a Black-Scholes valuation model to measure stock-based compensation expense at the date of grant. We adopted Statement of Financial Accounting Standards (SFAS) 123R, *Share-Based Payment*, under the modified prospective method in the first quarter of 2006. We do not expect our adoption of SFAS 123R to materially impact our financial statements.

Our divisions are held accountable for stock-based compensation expense and, therefore, this expense is allocated to our divisions as an incremental employee compensation cost. The allocation of stock-based compensation expense is approximately 29% to FLNA, 22% to PBNA, 31% to PI, 4% to QFNA and 14% to corporate unallocated expenses. The expense allocated to our divisions excludes any impact of changes in our Black-Scholes assumptions during the year which reflect market conditions over which division management has no control. Therefore, any variances between allocated expense and our actual expense are recognized in corporate unallocated expenses.

Our Assumptions

Our Black-Scholes model estimates the expected value our employees will receive from the options based on a number of assumptions, such as interest rates, employee exercises, our stock price and dividend yield. Our weighted-average fair value assumptions include:

	Estimated 2006	2005	2004	2003
Expected life	6 yrs.	6 yrs.	6 yrs.	6 yrs.
Risk free interest rate	3.8%	3.8%	3.3%	3.1%
Expected volatility	21%	23%	26%	27%
Expected dividend yield	1.9%	1.8%	1.8%	1.15%

The expected life is a significant assumption as it determines the period for which the risk free interest rate, volatility and dividend yield must be applied. The expected life is the period over which our employee groups are expected to hold their options. It is based on our historical experience with similar grants. The risk free interest rate is based on the expected U.S. Treasury rate over the expected life. Volatility reflects movements in our stock price over the most recent historical period equivalent to the expected life. Dividend yield is estimated over the expected life based on our stated dividend policy and forecasts of net income, share repurchases and stock price.

2006 Estimated Expense and Sensitivity of Assumptions

Our stock-based compensation expense, including RSUs, is as follows:

	Estimated 2006	2005	2004
Stock-based compensation expense	$296	$311	$368

If we assumed a 100 basis point change in the following assumptions, our estimated 2006 stock-based compensation expense would increase/(decrease) as follows:

	100 Basis Point Increase	100 Basis Point Decrease
Risk free interest rate	$6	$(6)
Expected volatility	$2	$(2)
Expected dividend yield	$(9)	$10

If the expected life were assumed to be one year longer, our estimated 2006 stock-based compensation expense would increase by $12 million. If the expected life were assumed to be one year shorter, our estimated 2006 stock-based compensation expense would decrease by $7 million. As noted, changing the assumed expected life impacts all of the Black-Scholes valuation assumptions as the risk free interest rate, expected volatility and expected dividend yield are estimated over the expected life.

Pension and Retiree Medical Plans

Our pension plans cover full-time employees in the U.S. and certain international employees. Benefits are determined based on either years of service or a combination of years of service and earnings. U.S. retirees are also eligible for medical and life insurance benefits (retiree medical) if they meet age and service requirements. Generally, our share of retiree medical costs is capped at specified dollar amounts that vary based upon years of service, with retirees contributing the remainder of the cost.

Our Assumptions

The determination of pension and retiree medical plan obligations and associated expenses requires the use of assumptions to estimate the amount of the benefits that employees earn while working, as well as the present value of those benefits. Annual pension and retiree medical expense amounts are principally based on four components: (1) the value of benefits earned by employees for working during the year (service cost), (2) increase in the liability due to the passage of time (interest cost), and (3) other gains and losses as discussed below, reduced by (4) expected return on plan assets for our funded plans.

The discount rate is based on interest rates for high-quality, long-term corporate debt securities with maturities comparable to our liabilities.

Significant assumptions used to measure our annual pension and retiree medical expense include:

- the interest rate used to determine the present value of liabilities (discount rate);
- certain employee-related factors, such as turnover, retirement age and mortality;
- for pension expense, the expected return on assets in our funded plans and the rate of salary increases for plans where benefits are based on earnings; and
- for retiree medical expense, health care cost trend rates.

Our assumptions reflect our historical experience and management's best judgment regarding future expectations. Some of these assumptions require significant management judgment and could have a material impact on the measurement of our pension and retiree medical benefit expenses and obligations. The assumptions used to measure our annual pension and retiree medical expenses are determined as of September 30 (measurement date) and all plan assets and liabilities are generally reported as of that date.

At each measurement date, the discount rate is based on interest rates for high-quality, long-term corporate debt securities with maturities comparable to our liabilities. In the U.S., we utilize the Moody's AA Corporate Index yield and adjust for the differences between the average duration of the bonds in this Index and the average duration of our benefits liabilities based upon a published index.

The expected return on pension plan assets is based on our historical experience, our pension plan investment strategy and our expectations for long-term rates of return. Our pension plan investment strategy is reviewed annually and is based upon plan liabilities, an evaluation of market conditions, tolerance for risk, and cash requirements for benefit payments. We use a third-party advisor to assist us in determining our investment allocation and modeling our long-term rate of return assumptions. Our current investment allocation target for our U.S. plans is 60% in equity securities, with the balance in fixed income securities and cash. Our expected long-term rate of return assumptions on U.S. plan assets is 7.8%, reflecting an estimated long-term return of 9.3% from equity securities and an estimated 5.8% from fixed income securities. Approximately 80% of our pension plan assets relate to our U.S. plans. We use a market-related value method that recognizes each year's asset gain or loss over a five-year period. Therefore, it takes five years for the gain or loss from any one year to be fully included in the other gains and losses calculation described below.

Other gains and losses resulting from actual experience differing from our assumptions and from changes in our assumptions are also determined at each measurement date. If this net accumulated gain or loss exceeds 10% of the greater of plan assets or liabilities, a portion of the net gain or loss is included in expense for the following year. The cost or benefit of plan changes which increase or decrease benefits for prior employee service (prior service cost) is included in expense on a straight-line basis over the average remaining service period of those expected to benefit, which is approximately 11 years for pension expense and approximately 13 years for retiree medical.

Weighted-average assumptions for pension and retiree medical expense are the following:

	2006	2005	2004
Pension			
Expense discount rate	5.6%	6.1%	6.1%
Expected rate of return on plan assets	7.7%	7.8%	7.8%
Expected rate of compensation increases	4.4%	4.3%	4.4%
Retiree medical			
Expense discount rate	5.7%	6.1%	6.1%
Current health care cost trend rate	10.0%	11.0%	12.0%

Future Expense

An analysis of the estimated change in pension and retiree medical expense follows:

	Pension	Retiree Medical
2005 expense	$329	$135
Decrease in discount rate	84	6
Increase in experience loss/(gain) amortization	69	(3)
Impact of contributions	(63)	–
Other, including impact of 2003 Medicare Act	(14)	(12)
2006 estimated expense	$405	$126

Our 2006 pension expense is estimated to be approximately $405 million and retiree medical expense is estimated to be approximately $126 million. These estimates incorporate the 2006 assumptions, as well as the impact of the increased pension plan assets resulting from our discretionary contributions of $729 million in 2005 and the impact of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Medicare Act) as discussed in Note 7. Changes in our 2006 assumptions include updates to the lump sum discount rate for the U.S. plans and to the mortality tables for certain international plans. The estimated increase of $69 million in net experience loss amortization included in estimated 2006 pension expense primarily reflects the recognition of lower than expected returns and past asset losses, which account for approximately $36 million of the increase, as well as assumption changes and demographic experience, which account for approximately $20 million of the increase.

Pension service costs, measured at a fixed discount rate but including the effect of demographic assumption changes, as well as the effects of gains and losses due to demographics, are reflected in division results. The effect of changes in discount and asset return rates, gains and losses other than those due to demographics, and the impact of funding are reflected in corporate unallocated expenses. Approximately $26 million of the increased pension and retiree medical expense in 2006 will be reflected in corporate unallocated expenses.

Based on our current assumptions which reflect our prior experience, current plan provisions, and expectations for future experience, and assuming the Board approves annual discretionary contributions of approximately $200 million, we expect our pension expense to remain relatively flat in 2007. In 2008, we expect our pension expense to begin to decline, with the expense dropping to approximately $305 million by 2011 as unrecognized experience losses are amortized. If our assumptions and our plan provisions for retiree medical remain unchanged and our experience mirrors these assumptions, we expect our annual retiree medical expense beyond 2006 to approximate $130 million.

Our 2006 pension expense is estimated to be approximately $405 million and retiree medical expense is estimated to be approximately $126 million.

Sensitivity of Assumptions

A decrease in the discount rate or in the expected rate of return assumptions would increase pension expense. The estimated impact of a 25 basis point decrease in the discount rate on 2006 pension expense is an increase of approximately $39 million. The estimated impact on 2006 pension expense of a 25 basis point decrease in the expected rate of return assumption is an increase of approximately $16 million. See Note 7 regarding the sensitivity of our retiree medical cost assumptions.

Future Funding

We make contributions to pension trusts maintained to provide plan benefits for certain pension plans. These contributions are made in accordance with applicable tax regulations that provide for current tax deductions for our contributions, and taxation to the employee only upon receipt of plan benefits. Generally, we do not fund our pension plans when our contributions would not be currently deductible.

Our pension contributions for 2005 were $803 million, of which $729 million was discretionary. In 2006, we expect contributions to be about $250 million with approximately $200 million expected to be discretionary. Our cash payments for retiree medical are estimated to be $85 million in 2006. As our retiree medical plans are not subject to regulatory funding requirements, we fund these plans on a pay-as-you-go basis. For estimated future benefit payments, including our pay-as-you-go payments as well as those from trusts, see Note 7.

Our Financial Results

Items Affecting Comparability

The year-over-year comparisons of our financial results are affected by the following items:

	2005	2004
Net revenue		
53rd week	**$418**	–
Operating profit		
53rd week	**$75**	–
2005 restructuring charges	**$(83)**	–
2004 restructuring and impairment charges	–	$(150)
Net income		
AJCA tax charge	**$(460)**	–
53rd week	**$57**	–
2005 restructuring charges	**$(55)**	–
2004 restructuring and impairment charges	–	$(96)
Net tax benefits — continuing operations	–	$266
Tax benefit from discontinued operations	–	$38
Net income per common share — diluted		
AJCA tax charge	**$(0.27)**	–
53rd week	**$0.03**	–
2005 restructuring charges	**$(0.03)**	–
2004 restructuring and impairment charges	–	$(0.06)
Net tax benefits — continuing operations	–	$0.15
Tax benefit from discontinued operations	–	$0.02

For the items and accounting changes affecting our 2003 results, see Note 1 and our 2003 Annual Report.

53rd week

In 2005, we had an additional week of results (53rd week). Our fiscal year ends on the last Saturday of each December, resulting in an additional week of results every five or six years.

2005 Restructuring Charges

In the fourth quarter of 2005, we incurred restructuring charges of $83 million to reduce costs in our operations, principally through headcount reductions.

2004 Restructuring and Impairment Charges

In the fourth quarter of 2004, we incurred restructuring and impairment charges of $150 million in conjunction with the consolidation of FLNA's manufacturing network in connection with its ongoing productivity program. Savings from this productivity program have been used to offset increased marketplace spending.

AJCA Tax Charge

As approved by our Board of Directors in July 2005, in the fourth quarter of 2005 we repatriated approximately $7.5 billion in earnings previously considered indefinitely reinvested outside the U.S. in connection with the AJCA. In 2005, we recorded income tax expense of $460 million associated with this repatriation.

Net Tax Benefits — Continuing Operations

In the fourth quarter of 2004, we recognized $45 million of tax benefits related to the completion of the U.S. Internal Revenue Service (IRS) audit for pre-merger Quaker open tax years. In the third quarter of 2004, we recognized $221 million of tax benefits related to a reduction in foreign tax accruals following the resolution of certain open tax issues with foreign tax authorities, and a refund claim related to prior U.S. tax settlements.

Tax Benefit from Discontinued Operations

In the fourth quarter of 2004, we reached agreement with the IRS for an open issue related to our discontinued restaurant operations which resulted in a tax benefit of $38 million.

Results of Continuing Operations — Consolidated Review

In the discussions of net revenue and operating profit below, effective net pricing reflects the year-over-year impact of discrete pricing actions, sales incentive activities and mix resulting from selling varying products in different package sizes and in different countries.

Servings

Since our divisions each use different measures of physical unit volume (i.e., kilos, pounds and case sales), a common servings metric is necessary to reflect our consolidated physical unit volume. Our divisions' physical volume measures are converted into servings based on U.S. Food and Drug Administration guidelines for single-serving sizes of our products.

Total servings increased 7% in 2005 compared to 2004 as servings for beverages worldwide grew over 7% and servings for snacks worldwide grew 6%. All of our divisions positively contributed to the total servings growth. Total servings increased 6% in 2004 compared to 2003 as servings for beverages worldwide grew 7% and servings for snacks worldwide grew over 5%.

Net Revenue and Operating Profit

				Change	
	2005	2004	2003	2005	2004
Division net revenues	$32,562	$29,261	$26,969	11%	8%
Divested businesses	–	–	2		
Total net revenue	$32,562	$29,261	$26,971	11%	8%
Division operating profit	$6,710	$6,098	$5,463	10%	12%
Corporate unallocated	(788)	(689)	(502)	14%	38%
Merger-related costs	–	–	(59)		
Impairment and restructuring charges	–	(150)	(147)		
Divested businesses	–	–	26		
Total operating profit	$5,922	$5,259	$4,781	13%	10%
Division operating profit margin	20.6%	20.8%	20.3%	(0.2)	0.5
Total operating profit margin	18.2%	18.0%	17.7%	0.2	0.3

2005

Net revenue increased 11% reflecting, across all divisions, increased volume, favorable effective net pricing, and net favorable foreign currency movements. The volume gains contributed 6 percentage points, the effective net pricing contributed 3 percentage points and the net favorable foreign currency movements contributed over 1 percentage point. The 53rd week contributed over 1 percentage point to revenue growth and almost 1 percentage point to volume growth.

Total operating profit increased 13% and margin increased 0.2 percentage points. Division operating profit increased 10% and margin decreased 0.2 percentage points. The operating profit gains primarily reflect leverage from the revenue growth, partially offset by higher selling and distribution (S&D) expenses and increased cost of sales, largely due to higher raw materials, energy, and S&D labor costs, as well as higher advertising and marketing expenses. In 2005, division operating profit margin reflects our current year restructuring actions, while total operating profit margin benefited from a favorable comparison to prior year restructuring and impairment charges. The additional week in 2005 contributed over 1 percentage point to both total and division operating profit growth.

2004

Division net revenue increased 8%, primarily due to strong volume gains across all divisions, favorable product mix, primarily at PBNA and PI, and net favorable foreign currency movements. The volume gains contributed over 4 percentage points, the favorable mix contributed almost 2 percentage points, and the net favorable foreign currency contributed almost 2 percentage points to division net revenue growth.

Total operating profit increased 10% and margin increased 0.3 percentage points. Division operating profit increased 12% and division margin increased 0.5 percentage points. These gains reflect leverage from the revenue growth, partially offset by increased selling, general and administrative expenses, primarily corporate unallocated expenses. In addition, total operating profit growth reflects the absence of merger-related costs in 2004.

Corporate Unallocated Expenses

Corporate unallocated expenses include the costs of our corporate headquarters, centrally managed initiatives such as our BPT initiative, unallocated insurance and benefit programs, foreign exchange transaction and certain commodity derivative gains and losses, as well as profit-in-inventory elimination adjustments for our noncontrolled bottling affiliates and certain other items.

In 2005, corporate unallocated expenses increased 14%. This increase primarily reflects higher costs associated with our BPT initiative which contributed 7 percentage points, increased support behind health and wellness and innovation initiatives which contributed 5 percentage points, and Corporate departmental expenses and restructuring charges which each contributed 2 percentage points to the increase. In 2005, items of a nonrecurring nature included charges of $55 million to conform our method of accounting across all divisions, primarily for warehouse and freight costs, and a gain of $25 million in connection with the

settlement of a class action lawsuit related to our purchases of high fructose corn syrup from 1991 to 1995. In 2004, we recorded a charge of $50 million for the settlement of a contractual dispute with a former business partner.

In 2004, corporate unallocated expenses increased 38%. Higher employee-related costs contributed 18 percentage points of the increase, an accrual recognized in the fourth quarter for the settlement of a contractual dispute with a former business partner represented 10 percentage points of the increase and higher costs related to our BPT initiative contributed 4 percentage points of the increase. Corporate departmental expenses increased 2% compared to prior year.

Other Consolidated Results

	2005	2004	2003	Change 2005	Change 2004
Bottling equity income	**$557**	$380	$323	**46%**	18%
Interest expense, net	**$(97)**	$(93)	$(112)	**4%**	(17)%
Annual tax rate	**36.1%**	24.7%	28.5%		
Net income — continuing operations	**$4,078**	$4,174	$3,568	**(2)%**	17%
Net income per common share — continuing operations — diluted	**$2.39**	$2.41	$2.05	**(1)%**	18%

Bottling equity income includes our share of the net income or loss of our noncontrolled bottling affiliates as described in "Our Customers." Our interest in these bottling investments may change from time to time. Any gains or losses from these changes, as well as other transactions related to our bottling investments, are also included on a pre-tax basis. We continue to sell shares of PBG stock to trim our ownership to the level at the time of PBG's initial public offering, since our ownership has increased as a result of PBG's share repurchase program. During 2005, we sold 7.5 million shares of PBG stock. The resulting lower ownership percentage reduces the equity income from PBG that we recognize.

2005

Bottling equity income increased 46% reflecting $126 million of pre-tax gains on our sales of PBG stock, as well as stronger bottler results. In the first quarter of 2006, PBG and PAS adopted SFAS 123R which will negatively impact our bottling equity income.

Net interest expense increased 4% reflecting the impact of higher debt levels, substantially offset by higher investment rates and cash balances.

The tax rate increased 11.4 percentage points reflecting the $460 million tax charge related to our repatriation of undistributed international earnings, as well as the absence of income tax benefits of $266 million recorded in the prior year related to a reduction in foreign tax accruals following the resolution of certain open tax items with foreign tax authorities and a refund claim related to prior U.S. tax settlements. This increase was partially offset by increased international profit which is taxed at a lower rate.

Net income from continuing operations decreased 2% and the related net income per common share from continuing operations decreased 1%. These decreases reflect the impact of the tax items discussed above, partially offset by our operating profit growth, increased bottling equity income, which includes the gain on our PBG stock sale, the impact of the 53rd week, a favorable comparison to prior year restructuring and impairment charges, and for net income per share, the impact of our share repurchases.

2004

Bottling equity income increased 18%, primarily reflecting increased earnings from our anchor bottlers and favorable comparisons from international bottling investments, primarily as a result of the nationwide strike in Venezuela in early 2003.

Net interest expense declined 17% primarily due to favorable interest rates and higher average cash balances, partially offset by higher average debt balances and lower gains in the market value of investments used to economically hedge a portion of our deferred compensation liability. The offsetting increase in deferred compensation costs is reported in corporate unallocated expenses.

The annual tax rate decreased 3.8 percentage points compared to the prior year, primarily as a result of tax benefits from the resolution of open items with tax authorities in both years, as discussed in "Items Affecting Comparability." The tax benefits reduced our tax rate by 2.6 percentage points. Increased benefit from concentrate operations and favorable changes arising from agreements with the IRS in the fourth quarter of 2003 also contributed to the decline in rate.

Net income from continuing operations increased 17% and the related net income per common share from continuing operations increased 18%. These increases primarily reflect the solid operating profit growth and our lower annual tax rate. The absence of merger-related costs in 2004 and increased bottling equity income also contributed to the growth.

Results of Continuing Operations — Division Review

The results and discussions below are based on how our Chief Executive Officer monitors the performance of our divisions. Prior year amounts exclude the results of divested businesses. For additional information on these items and our divisions, see Note 1.

	FLNA	PBNA	PI	QFNA	Total
Net Revenue, 2005	**$10,322**	**$9,146**	**$11,376**	**$1,718**	**$32,562**
Net Revenue, 2004	$9,560	$8,313	$9,862	$1,526	$29,261
% Impact of:					
Volume	4.5%	4%(a)	8%(a)	9%	6%
Effective net pricing	3	5	2.5	3	3
Foreign exchange	0.5	–	3	1	1
Acquisition/divestitures	–	–	2	–	0.5
% Change(b)	*8%*	*10%*	*15%*	*13%*	*11%*

	FLNA	PBNA	PI	QFNA	Divested Businesses	Total
Net Revenue, 2004	$9,560	$8,313	$9,862	$1,526	–	$29,261
Net Revenue, 2003	$9,091	$7,733	$8,678	$1,467	$2	$26,971
% Impact of:						
Volume	3%	3%(a)	7%(a)	3%	–	4%
Effective net pricing	2	4	2	–	–	2
Foreign exchange	–	–	4	1	–	2
Acquisition/divestitures	–	–	1	–	–	–
% Change(b)	*5%*	*7%*	*14%*	*4%*	*N/A*	*8%*

(a) For beverages sold to our bottlers, net revenue volume growth is based on our concentrate shipments and equivalents.

(b) Amounts may not sum due to rounding.

Frito-Lay North America

	2005	2004	2003	% Change 2005	% Change 2004
Net revenue	$10,322	$9,560	$9,091	8	5
Operating profit	$2,529	$2,389	$2,242	6	7

2005

Net revenue grew 8% reflecting volume growth of 4.5% and positive effective net pricing driven by salty snack pricing actions and favorable mix on both salty and convenience foods products. Pound volume grew primarily due to mid single-digit growth in trademark Lay's potato chips, high single-digit growth in salty trademark Tostitos, double-digit growth in Santitas, mid single-digit growth in trademark Cheetos, high single-digit growth in Dips and Fritos, and double-digit growth in Sun Chips. These gains were partially offset by the discontinuance of Toastables and Doritos Rollitos. Overall, salty snacks revenue grew 8% with volume growth of 5%, and convenience foods products revenue grew 13% with volume growth of 1%. Convenience foods products revenue benefited from favorable mix. The additional week contributed 2 percentage points to volume and net revenue growth.

Operating profit grew 6% reflecting positive effective net pricing actions and volume growth. This growth was offset by higher S&D costs resulting from increased labor and benefit charges and fuel costs; higher cost of sales, driven by raw materials, natural gas and freight; and increased advertising and marketing costs. Operating profit was also negatively impacted by more than 1 percentage point as a result of fourth quarter charges to reduce costs in our operations, principally through headcount reductions. The additional week contributed 2 percentage points to operating profit growth.

FLNA volume grew 4.5% in 2005 and 3% in 2004.

Products qualifying for our new Smart Spot program represented approximately 13% of net revenue. These products experienced double-digit revenue growth, while the balance of the portfolio had high single-digit revenue growth. See our website at www.smartspot.com for additional information on our Smart Spot program.

2004

Net revenue grew 5% reflecting volume growth of 3% and positive effective net pricing due to salty snack pricing actions and favorable mix. Pound volume grew primarily due to new products, single-digit growth in Lay's Classic potato chips, strong double-digit growth in Variety Pack and mid single-digit growth in Tostitos and Fried Cheetos. Lay's Stax and Doritos Rollitos led the new product growth. These gains were partially offset by single-digit declines in Doritos and Fritos and double-digit declines in Rold Gold and Quaker Toastables.

Operating profit grew nearly 7% reflecting the positive pricing actions and volume growth. Higher commodity costs, driven by corn oil and energy costs were largely offset by cost leverage generated from ongoing productivity initiatives.

Smart Spot eligible products represented approximately 10% of 2004 FLNA net revenue. These products experienced high single-digit revenue growth and the balance of the portfolio had mid single-digit revenue growth.

PepsiCo Beverages North America

				% Change	
	2005	2004	2003	2005	2004
Net revenue	$9,146	$8,313	$7,733	10	7
Operating profit	$2,037	$1,911	$1,690	7	13

2005

Net revenue grew 10% and volume grew 4%. The volume increase was driven by a 16% increase in non-carbonated beverages, partially offset by a 1% decline in CSDs. Within non-carbonated beverages, Gatorade, Trademark Aquafina, Tropicana juice drinks, Propel and SoBe all experienced double-digit growth. Above average summer temperatures across the country, as well as the launch of new products such as Aquafina FlavorSplash and Gatorade Lemonade earlier in the year, drove Gatorade and Trademark Aquafina growth. Tropicana Pure Premium experienced a low single-digit decline resulting from price increases taken in the first quarter. The decline in CSDs reflects low single-digit declines in Trademark Pepsi and Trademark Mountain Dew, slightly offset by low single-digit growth in Sierra Mist. Across the brands, a low single-digit decline in regular CSDs was partially offset by low single-digit growth in diet CSDs. The additional week in 2005 had no significant impact on volume growth as bottler volume is reported based on a calendar month.

Gatorade, Trademark Aquafina, Tropicana juice drinks, Propel and SoBe all experienced double-digit volume growth in 2005.

Net revenue also benefited from 5 percentage points of favorable effective net pricing, reflecting the continued migration from CSDs to non-carbonated beverages and price increases taken in the first quarter, primarily on concentrate and Tropicana Pure Premium, partially offset by increased trade spending in the current year. The additional week in 2005 contributed 1 percentage point to net revenue growth.

Operating profit increased nearly 7%, primarily reflecting net revenue growth. This increase was partially offset by higher raw material, energy, and transportation costs, as well as increased advertising and marketing expenses. The additional week in 2005 contributed 1 percentage point to operating profit growth and was fully offset by a 1 percentage point decline related to charges taken in the fourth quarter of 2005 to reduce costs in our operations, principally through headcount reductions.

Smart Spot eligible products represented almost 70% of net revenue. These products experienced double-digit revenue growth, while the balance of the portfolio grew in the low single-digit range.

2004

Net revenue increased 7% and volume increased 3%. The volume increase reflects non-carbonated beverage growth of 10% and a slight increase in CSDs. The non-carbonated beverage growth was fueled by double-digit growth in Gatorade, Aquafina and Propel, as well as the introduction of bottler-distributed Tropicana juice drinks. Tropicana Pure Premium increased slightly for the year. The carbonated soft drink performance reflects a low single-digit increase in Trademark Mountain Dew and a slight increase in Trademark Sierra Mist, offset by a slight decline in Trademark Pepsi. Across the trademarks, high single-digit diet CSD growth was substantially offset by a low single-digit decline in regular CSDs. The increase in Trademark Mountain Dew reflects growth in both Diet and regular Mountain Dew and the limited time only offering of Mountain Dew Pitch Black, substantially offset by declines in both Mountain Dew Code Red and LiveWire. The performance of Trademark Pepsi reflects declines in regular Pepsi, Pepsi Twist and Pepsi Blue, mostly offset by increases in Diet Pepsi and the introduction of Pepsi Edge. Favorable product mix contributed 3 percentage points to net revenue growth, primarily reflecting a migration to non-carbonated beverages. Additionally, concentrate and fountain price increases taken in the first quarter contributed 1 percentage point to net revenue growth.

Operating profit increased 13% reflecting the net revenue growth, partially offset by higher selling, general and administrative costs, as well as costs related to marketplace initiatives.

Smart Spot eligible products represented over 60% of net revenue. These products experienced high single-digit revenue growth, and the balance of the portfolio had mid single-digit revenue growth.

PepsiCo International

	2005	2004	2003	% Change 2005	% Change 2004
Net revenue	$11,376	$9,862	$8,678	15	14
Operating profit	$1,607	$1,323	$1,061	21	25

2005

International snacks volume grew 7%, reflecting growth of 11% in the Europe, Middle East & Africa region, 5% in the Latin America region and 6% in the Asia Pacific region. Acquisition and divestiture activity, principally the divestiture last year of our interest in a South Korea joint venture, reduced Asia region volume by 11 percentage points. The acquisition of a business in Romania late in 2004 increased the Europe, Middle East & Africa region volume growth by 3 percentage points. Cumulatively, our divestiture and acquisition activities did not impact the reported total PepsiCo International snack volume growth rate. The overall gains reflected mid single-digit growth at Sabritas in Mexico, double-digit growth in India, Turkey, Russia, Australia and China, partially offset by a low single-digit decline at Walkers in the United Kingdom. The decline at Walkers is due principally to marketplace pressures. The additional week contributed 1 percentage point to international snack volume growth.

Beverage volume grew 11%, reflecting growth of 14% in the Europe, Middle East & Africa region, 11% in the Asia Pacific region and 6% in the Latin America region. Acquisitions had no significant impact on the reported total PepsiCo International beverage volume growth rate. Broad-based increases were led by double-digit growth in the Middle East, China, Argentina, Venezuela and Russia. Carbonated soft drinks and non-carbonated beverages both grew at a double-digit rate. The additional week had no impact on beverage volume growth as volume is reported based on a calendar month.

Net revenue grew 15%, primarily as a result of the broad-based volume growth and favorable effective net pricing. Foreign currency contributed almost 3 percentage points of growth reflecting the favorable Mexican peso and Brazilian real, partially offset by the unfavorable British pound. Acquisitions and divestitures contributed almost 2 percentage points of growth. The additional week contributed 1 percentage point to revenue growth. Cumulatively, the impact of foreign currency, acquisitions and divestitures, and the additional week on net revenue was 5 percentage points.

Operating profit grew 21% driven largely by the broad-based volume growth and favorable effective net pricing, partially offset by increased energy and raw material costs. Foreign currency contributed 4 percentage points of growth based on the favorable Mexican peso and Brazilian real. The net favorable impact from acquisition and divestiture activity, primarily the acquisition of General Mills' minority interest in Snack Ventures Europe in Q1 2005, contributed 2 percentage points of growth. The additional week contributed 1 percentage point to operating profit growth which was fully offset by a 1 percentage point decline in operating profit growth related to fourth quarter charges to reduce costs in our operations and rationalize capacity.

International snacks volume grew 7% and international beverage volume grew 11% in 2005.

2004

International snacks volume grew 8%, comprised of 7% in our Latin America region, 8% in our Europe, Middle East & Africa region and 14% in our Asia Pacific region. These gains were driven by high single-digit growth at Sabritas in Mexico, strong double-digit growth in India, low single-digit growth at Gamesa in Mexico coupled with double-digit growth in Egypt, Venezuela, Turkey and Brazil.

Beverage volume grew 12%, comprised of 14% in our Europe, Middle East & Africa region, 15% in our Asia Pacific region and 8% in our Latin America region. Broad-based increases were led by double-digit growth in the Middle East and China, high single-digit growth in Mexico and double-digit growth in India, Germany, Russia and Venezuela. Favorable comparisons as a result of the 2003 national strike in Venezuela and the German deposit law impact contributed to the growth in Venezuela and Germany. Both carbonated soft drinks and non-carbonated beverages grew at double-digit rates.

Net revenue grew 14% driven by the broad-based volume growth and favorable mix. Foreign currency impact contributed 4 percentage points of growth driven by the favorable British pound and euro, partially offset by the unfavorable Mexican peso. Acquisitions contributed less than 1 percentage point.

Operating profit grew 25% driven largely by the volume and favorable mix. The favorable comparison of certain reserve actions taken in 2003 on potentially unrecoverable beverage assets contributed 2 percentage points of growth. Foreign currency impact contributed almost 3 percentage points of growth driven by the favorable British pound and euro, partially offset by the unfavorable Mexican peso.

Quaker Foods North America

				% Change	
	2005	2004	2003	2005	2004
Net revenue	$1,718	$1,526	$1,467	13	4
Operating profit	$537	$475	$470	13	1

2005

Net revenue increased 13% and volume increased 9%. The volume increase reflects double-digit growth in Oatmeal, Aunt Jemima syrup and mix, Rice-A-Roni and Pasta Roni, as well as high single-digit growth in Cap'n Crunch cereal and mid single-digit growth in Life cereal. Higher effective net pricing contributed nearly 3 percentage points of growth reflecting favorable product mix, the settlement of prior year trade spending accruals and price increases on ready-to-eat cereals taken in the third quarter of 2004. Favorable Canadian exchange rates contributed nearly 1 percentage point to net revenue growth. The additional week in 2005 contributed approximately 2 percentage points to both net revenue and volume growth.

Operating profit increased 13% reflecting the net revenue growth. This growth was partially offset by higher advertising and marketing costs behind programs for core brands and innovation, as well as an unfavorable cost of sales comparison primarily due to higher energy and raw materials costs in the latter part of 2005. The additional week in 2005 contributed approximately 2 percentage points to operating profit growth.

QFNA volume increased 9% in 2005 reflecting double-digit growth in Oatmeal, Aunt Jemima syrup and mix, Rice-A-Roni and Pasta Roni.

Smart Spot eligible products represented approximately half of net revenue and had double-digit revenue growth. The balance of the portfolio also experienced double-digit revenue growth.

2004

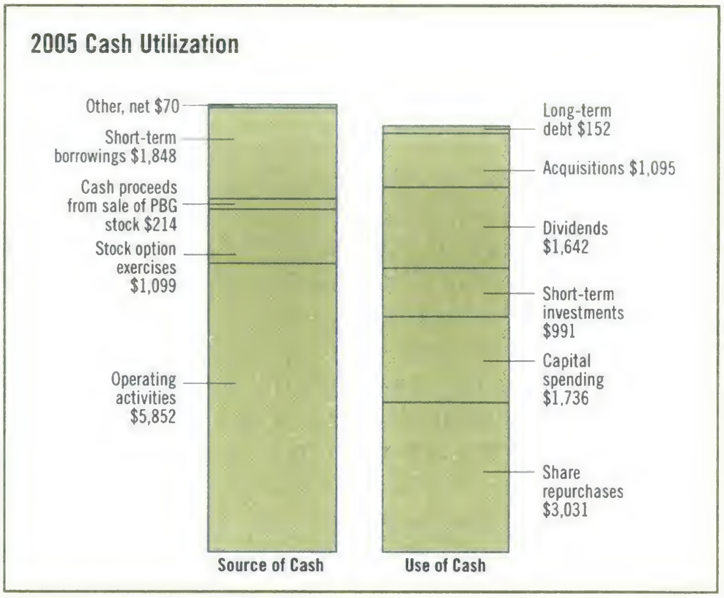
Net revenue increased 4% and volume increased 3%. The volume increase reflects high single-digit growth in Oatmeal and double-digit growth in Life cereal, partially offset by a mid single-digit decline in Cap'n Crunch cereal. The Life cereal growth was led by the introduction of Honey Graham Life. Favorable product mix, reflecting growth in higher revenue per pound brands, was offset by promotional spending behind new products. Favorable Canadian exchange rates contributed 1 percentage point to net revenue growth.

Operating profit increased 1% reflecting the net revenue growth, substantially offset by an unfavorable cost of sales comparison and higher advertising and marketing costs.

Smart Spot eligible products represented approximately half of net revenue and had high single-digit revenue growth. The balance of the portfolio was flat.

Our Liquidity, Capital Resources and Financial Position

Our strong cash-generating capability and financial condition give us ready access to capital markets throughout the world. Our principal source of liquidity is our operating cash flow. This cash-generating capability is one of our fundamental strengths and provides us with substantial financial flexibility in meeting operating, investing and financing needs. In addition, we have revolving credit facilities that are further discussed in Note 9. Our cash provided from operating activities is somewhat impacted by seasonality. Working capital needs are impacted by weekly sales, which are generally highest in the third quarter due to seasonal and holiday-related sales patterns, and generally lowest in the first quarter.



Operating Activities

In 2005, our operations provided $5.9 billion of cash compared to $5.1 billion in the prior year. The increase reflects our solid business results, as well as lower taxes paid in the current year as 2004 tax payments included a $760 million tax payment related to our 2003 settlement with the IRS. This increase was partially offset by $803 million of pension plan contributions in the current year, of which $729 million was discretionary, compared to pension payments of $458 million in the prior year, of which $400 million was discretionary.

Investing Activities

In 2005, we used $3.5 billion, primarily reflecting capital spending of $1.7 billion, acquisitions of $1.1 billion, primarily the $750 million acquisition of General Mills' minority interest in Snack Ventures Europe, and net purchases of short-term investments of $1.0 billion. These amounts were partially offset by the proceeds from our sale of PBG stock of $214 million. In 2004, we used $2.3 billion for investing, primarily reflecting capital spending of $1.4 billion and short-term investments of almost $1.0 billion.

In the first quarter of 2006, we completed our acquisition of Stacy's Pita Chip Company which was funded with existing domestic cash. This acquisition will be included in the first quarter of 2006 as an investing activity in our Condensed Consolidated Statement of Cash Flows.

We anticipate net capital spending of approximately $2.2 billion in 2006, which is above our long-term target of approximately 5% of net revenue. Planned capital spending in 2006 includes increased investments in manufacturing capacity to support growth in our China snack and beverage operations and our North American Gatorade business, as well as increased investment in support of our ongoing BPT initiative. We expect capital spending to return to our long-term targeted rate following 2006.

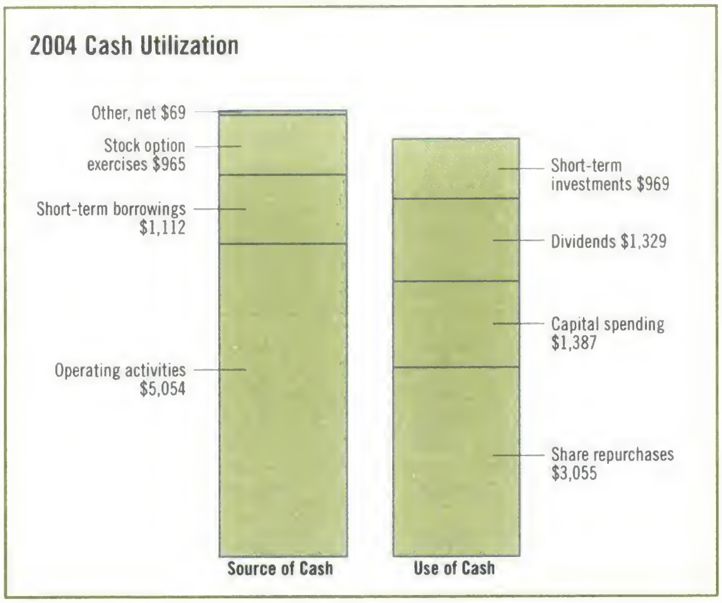
Financing Activities

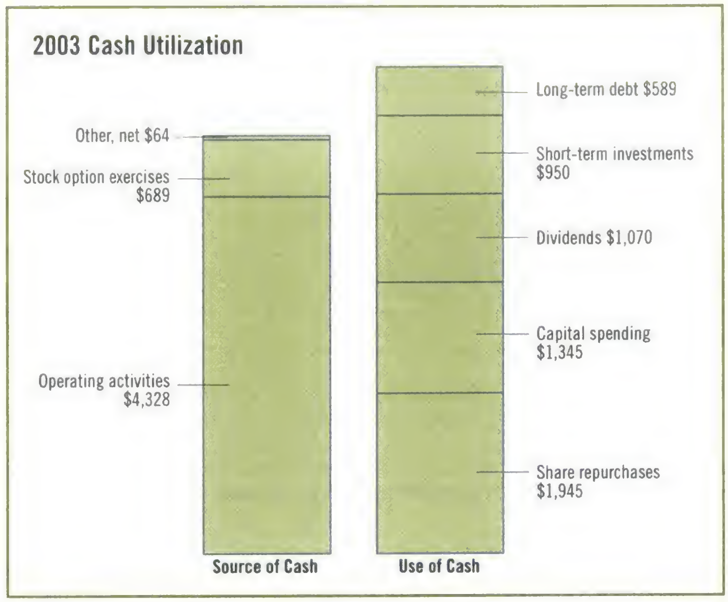
In 2005, we used $1.9 billion, primarily reflecting common share repurchases of $3.0 billion and dividend payments of $1.6 billion, partially offset by net proceeds from short-term borrowings of $1.8 billion and stock option proceeds of $1.1 billion. This compares to $2.3 billion used for financing in 2004, primarily reflecting share repurchases at a cost of $3.0 billion and dividend payments of $1.3 billion, partially offset by net issuances of short-term borrowings of $1.1 billion and proceeds from exercises of stock options of nearly $1.0 billion.

In 2004, our Board of Directors authorized a new $7.0 billion share repurchase program. Since inception of the new program, we have repurchased $5.1 billion of shares, leaving $1.9 billion of remaining authorization. We target an annual dividend payout of approximately 45% of prior year's net income from continuing operations. Each spring we review our capital structure with our Board, including our dividend policy and share repurchase activity.

Management Operating Cash Flow

We focus on management operating cash flow as a key element in achieving maximum shareholder value, and it is the primary measure we use to monitor cash flow performance. However, it is not a measure provided by accounting principles generally accepted in the U.S. Since net capital spending is essential to our product innovation initiatives and maintaining our operational capabilities, we believe that it is a recurring and necessary use of cash. As such, we believe investors should also consider net capital spending when evaluating our cash from operating activities.





The table below reconciles the net cash provided by operating activities as reflected in our Consolidated Statement of Cash Flows to our management operating cash flow.

	2005	2004	2003
Net cash provided by operating activities	**$ 5,852**	$ 5,054	$ 4,328
Capital spending	**(1,736)**	(1,387)	(1,345)
Sales of property, plant and equipment	**88**	38	49
Management operating cash flow	**$ 4,204**	$ 3,705	$ 3,032

Management operating cash flow was used primarily to repurchase shares and pay dividends. We expect to continue to return approximately all of our management operating cash flow to our shareholders through dividends and share repurchases. However, see "Our Business Risks" for certain factors that may impact our operating cash flows.

Credit Ratings

Our debt ratings of Aa3 from Moody's and A+ from Standard & Poor's contribute to our ability to access global capital markets. We have maintained strong investment grade ratings for over a decade. Our Moody's rating reflects an upgrade from A1 to Aa3 in 2004 due to the strength of our balance sheet and cash flows. Each rating is considered strong investment grade and is in the first quartile of their respective ranking systems. These ratings also reflect the impact of our anchor bottlers' cash flows and debt.

Credit Facilities and Long-Term Contractual Commitments

See Note 9 for a description of our credit facilities and long-term contractual commitments.

Off-Balance Sheet Arrangements

It is not our business practice to enter into off-balance sheet arrangements, other than in the normal course of business, nor is it our policy to issue guarantees to our bottlers, noncontrolled affiliates or third parties. However, certain guarantees were necessary to facilitate the separation of our bottling and restaurant operations from us. As of year-end 2005, we believe it is remote that these guarantees would require any cash payment. See Note 9 for a description of our off-balance sheet arrangements.

Financial Position

Significant changes in our Consolidated Balance Sheet from December 25, 2004 to December 31, 2005 not discussed above were as follows:

- Other assets increased primarily reflecting our increased pension contributions in the current year.
- Income taxes payable increased primarily reflecting $460 million of taxes accrued related to our repatriation of international earnings in connection with the AJCA to be paid in the first quarter of 2006.

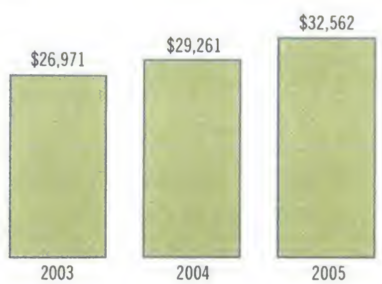
Consolidated Statement of Income

PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 31, 2005, December 25, 2004 and December 27, 2003

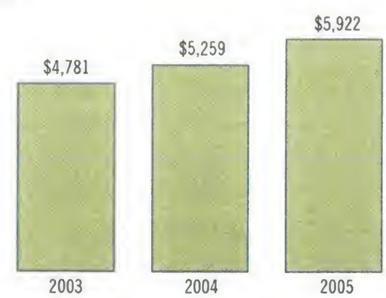
(in millions except per share amounts)	2005	2004	2003
Net Revenue	$32,562	$29,261	$26,971
Cost of sales	14,176	12,674	11,691
Selling, general and administrative expenses	12,314	11,031	10,148
Amortization of intangible assets	150	147	145
Restructuring and impairment charges	–	150	147
Merger-related costs	–	–	59
Operating Profit	5,922	5,259	4,781
Bottling equity income	557	380	323
Interest expense	(256)	(167)	(163)
Interest income	159	74	51
Income from Continuing Operations before Income Taxes	6,382	5,546	4,992
Provision for Income Taxes	2,304	1,372	1,424
Income from Continuing Operations	4,078	4,174	3,568
Tax Benefit from Discontinued Operations	–	38	–
Net Income	$ 4,078	$ 4,212	$ 3,568
Net Income per Common Share — Basic			
Continuing operations	$2.43	$2.45	$2.07
Discontinued operations	–	0.02	–
Total	$2.43	$2.47	$2.07
Net Income per Common Share — Diluted			
Continuing operations	$2.39	$2.41	$2.05
Discontinued operations	–	0.02	–
Total	$2.39	$2.44*	$2.05

* Based on unrounded amounts.
See accompanying notes to consolidated financial statements.

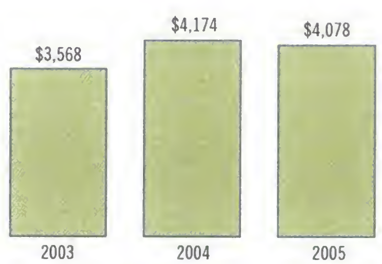
Net Revenue



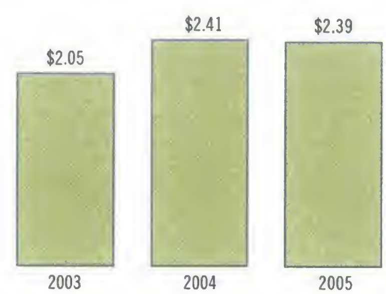
Operating Profit



Income from Continuing Operations



Net Income per Common Share — Continuing Operations



Consolidated Statement of Cash Flows

PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 31, 2005, December 25, 2004 and December 27, 2003

(in millions)	2005	2004	2003
Operating Activities			
Net income	$ 4,078	$ 4,212	$ 3,568
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	1,308	1,264	1,221
Stock-based compensation expense	311	368	407
Restructuring and impairment charges	–	150	147
Cash payments for merger-related costs and restructuring charges	(22)	(92)	(109)
Tax benefit from discontinued operations	–	(38)	–
Pension and retiree medical plan contributions	(877)	(534)	(605)
Pension and retiree medical plan expenses	464	395	277
Bottling equity income, net of dividends	(411)	(297)	(276)
Deferred income taxes and other tax charges and credits	440	(203)	(286)
Merger-related costs	–	–	59
Other non-cash charges and credits, net	145	166	101
Changes in operating working capital, excluding effects of acquisitions and divestitures			
Accounts and notes receivable	(272)	(130)	(220)
Inventories	(132)	(100)	(49)
Prepaid expenses and other current assets	(56)	(31)	23
Accounts payable and other current liabilities	188	216	(11)
Income taxes payable	609	(268)	182
Net change in operating working capital	337	(313)	(75)
Other	79	(24)	(101)
Net Cash Provided by Operating Activities	5,852	5,054	4,328
Investing Activities			
Snack Ventures Europe (SVE) minority interest acquisition	(750)	–	–
Capital spending	(1,736)	(1,387)	(1,345)
Sales of property, plant and equipment	88	38	49
Other acquisitions and investments in noncontrolled affiliates	(345)	(64)	(71)
Cash proceeds from sale of PBG stock	214	–	–
Divestitures	3	52	46
Short-term investments, by original maturity			
More than three months — purchases	(83)	(44)	(38)
More than three months — maturities	84	38	28
Three months or less, net	(992)	(963)	(940)
Net Cash Used for Investing Activities	(3,517)	(2,330)	(2,271)
Financing Activities			
Proceeds from issuances of long-term debt	25	504	52
Payments of long-term debt	(177)	(512)	(641)
Short-term borrowings, by original maturity			
More than three months — proceeds	332	153	88
More than three months — payments	(85)	(160)	(115)
Three months or less, net	1,601	1,119	40
Cash dividends paid	(1,642)	(1,329)	(1,070)
Share repurchases — common	(3,012)	(3,028)	(1,929)
Share repurchases — preferred	(19)	(27)	(16)
Proceeds from exercises of stock options	1,099	965	689
Net Cash Used for Financing Activities	(1,878)	(2,315)	(2,902)
Effect of exchange rate changes on cash and cash equivalents	(21)	51	27
Net Increase/(Decrease) in Cash and Cash Equivalents	436	460	(818)
Cash and Cash Equivalents, Beginning of Year	1,280	820	1,638
Cash and Cash Equivalents, End of Year	$ 1,716	$ 1,280	$ 820

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

PepsiCo, Inc. and Subsidiaries
December 31, 2005 and December 25, 2004

(in millions except per share amounts)	2005	2004
ASSETS		
Current Assets		
Cash and cash equivalents	$ 1,716	$ 1,280
Short-term investments	3,166	2,165
	4,882	3,445
Accounts and notes receivable, net	3,261	2,999
Inventories	1,693	1,541
Prepaid expenses and other current assets	618	654
Total Current Assets	10,454	8,639
Property, Plant and Equipment, net	8,681	8,149
Amortizable Intangible Assets, net	530	598
Goodwill	4,088	3,909
Other nonamortizable intangible assets	1,086	933
Nonamortizable Intangible Assets	5,174	4,842
Investments in Noncontrolled Affiliates	3,485	3,284
Other Assets	3,403	2,475
Total Assets	$31,727	$27,987
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Short-term obligations	$ 2,889	$ 1,054
Accounts payable and other current liabilities	5,971	5,599
Income taxes payable	546	99
Total Current Liabilities	9,406	6,752
Long-Term Debt Obligations	2,313	2,397
Other Liabilities	4,323	4,099
Deferred Income Taxes	1,434	1,216
Total Liabilities	17,476	14,464
Commitments and Contingencies		
Preferred Stock, no par value	41	41
Repurchased Preferred Stock	(110)	(90)
Common Shareholders' Equity		
Common stock, par value 1 2/3¢ per share (issued 1,782 shares)	30	30
Capital in excess of par value	614	618
Retained earnings	21,116	18,730
Accumulated other comprehensive loss	(1,053)	(886)
	20,707	18,492
Less: repurchased common stock, at cost (126 and 103 shares, respectively)	(6,387)	(4,920)
Total Common Shareholders' Equity	14,320	13,572
Total Liabilities and Shareholders' Equity	$31,727	$27,987

See accompanying notes to consolidated financial statements.

Consolidated Statement of Common Shareholders' Equity

PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 31, 2005, December 25, 2004 and December 27, 2003

(in millions)	2005		2004		2003	
	Shares	Amount	Shares	Amount	Shares	Amount
Common Stock	1,782	$ 30	1,782	$ 30	1,782	$ 30
Capital in Excess of Par Value						
Balance, beginning of year		618		548		207
Stock-based compensation expense		311		368		407
Stock option exercises[a]		(315)		(298)		(66)
Balance, end of year		614		618		548
Retained Earnings						
Balance, beginning of year		18,730		15,961		13,489
Net income		4,078		4,212		3,568
Cash dividends declared — common		(1,684)		(1,438)		(1,082)
Cash dividends declared — preferred		(3)		(3)		(3)
Cash dividends declared — RSUs		(5)		(2)		–
Other		–		–		(11)
Balance, end of year		21,116		18,730		15,961
Accumulated Other Comprehensive Loss						
Balance, beginning of year		(886)		(1,267)		(1,672)
Currency translation adjustment		(251)		401		410
Cash flow hedges, net of tax:						
Net derivative gains/(losses)		54		(16)		(11)
Reclassification of (gains)/losses to net income		(8)		9		(1)
Minimum pension liability adjustment, net of tax		16		(19)		7
Unrealized gain on securities, net of tax		24		6		1
Other		(2)		–		(1)
Balance, end of year		(1,053)		(886)		(1,267)
Repurchased Common Stock						
Balance, beginning of year	(103)	(4,920)	(77)	(3,376)	(60)	(2,524)
Share repurchases	(54)	(2,995)	(58)	(2,994)	(43)	(1,946)
Stock option exercises	31	1,523	32	1,434	26	1,096
Other	–	5	–	16	–	(2)
Balance, end of year	(126)	(6,387)	(103)	(4,920)	(77)	(3,376)
Total Common Shareholders' Equity		$14,320		$13,572		$11,896

	2005	2004	2003
Comprehensive Income			
Net income	$4,078	$4,212	$3,568
Currency translation adjustment	(251)	401	410
Cash flow hedges, net of tax	46	(7)	(12)
Minimum pension liability adjustment, net of tax	16	(19)	7
Unrealized gain on securities, net of tax	24	6	1
Other	(2)	–	(1)
Total Comprehensive Income	$3,911	$4,593	$3,973

(a) Includes total tax benefit of $125 million in 2005, $183 million in 2004 and $340 million in 2003.
See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1 — Basis of Presentation and Our Divisions

Basis of Presentation

Our financial statements include the consolidated accounts of PepsiCo, Inc. and the affiliates that we control. In addition, we include our share of the results of certain other affiliates based on our economic ownership interest. We do not control these other affiliates, as our ownership in these other affiliates is generally less than 50%. Our share of the net income of noncontrolled bottling affiliates is reported in our income statement as bottling equity income. Bottling equity income also includes any changes in our ownership interests of these affiliates. In 2005, bottling equity income includes $126 million of pre-tax gains on our sales of PBG stock. See Note 8 for additional information on our noncontrolled bottling affiliates. Our share of other noncontrolled affiliates is included in division operating profit. Intercompany balances and transactions are eliminated. In 2005, we had an additional week of results (53rd week). Our fiscal year ends on the last Saturday of each December, resulting in an additional week of results every five or six years.

In connection with our ongoing BPT initiative, we aligned certain accounting policies across our divisions in 2005. We conformed our methodology for calculating our bad debt reserves and modified our policy for recognizing revenue for products shipped to customers by third-party carriers. Additionally, we conformed our method of accounting for certain costs, primarily warehouse and freight. These changes reduced our net revenue by $36 million and our operating profit by $60 million in 2005. We also made certain reclassifications on our Consolidated Statement of Income in the fourth quarter of 2005 from cost of sales to selling, general and administrative expenses in connection with our BPT initiative. These reclassifications resulted in reductions to cost of sales of $556 million through the third quarter of 2005, $732 million in the full year 2004 and $688 million in the full year 2003, with corresponding increases to selling, general and administrative expenses in those periods. These reclassifications had no net impact on operating profit and have been made to all periods presented for comparability.

The preparation of our consolidated financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect reported amounts of assets, liabilities, revenues, expenses and disclosure of contingent assets and liabilities. Estimates are used in determining, among other items, sales incentives accruals, future cash flows associated with impairment testing for perpetual brands and goodwill, useful lives for intangible assets, tax reserves, stock-based compensation and pension and retiree medical accruals. Actual results could differ from these estimates.

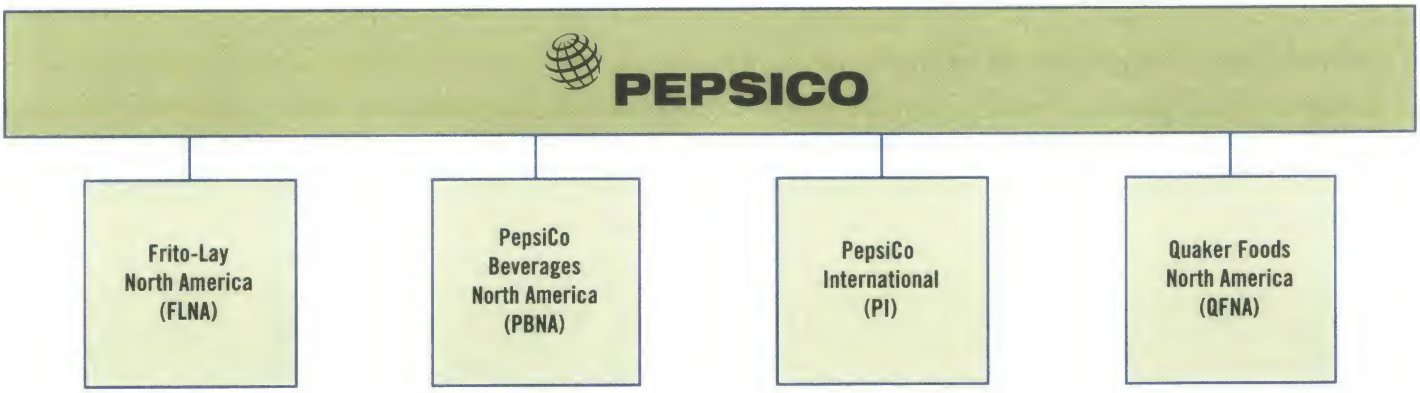
See "Our Divisions" below and for additional unaudited information on items affecting the comparability of our consolidated results, see "Items Affecting Comparability" in Management's Discussion and Analysis.

Tabular dollars are in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless noted, and are based on unrounded amounts. Certain reclassifications were made to prior years' amounts to conform to the 2005 presentation.

Our Divisions

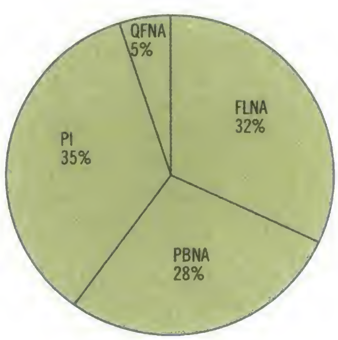
We manufacture or use contract manufacturers, market and sell a variety of salty, sweet and grain-based snacks, carbonated and non-carbonated beverages, and foods through our North American and international business divisions. Our North American divisions include the United States and Canada. The accounting policies for the divisions are the same as those described in Note 2, except for certain allocation methodologies for stock-based compensation expense and pension and retiree medical expense, as described in the unaudited information in "Our Critical Accounting Policies." Additionally, beginning in the fourth quarter of 2005, we began centrally managing commodity derivatives on behalf of our divisions. Certain of the commodity derivatives, primarily those related to the purchase of energy for use by our divisions, do not qualify for hedge accounting treatment. These derivatives hedge underlying commodity price risk and were not entered into for speculative purposes. Such derivatives are marked to market with the resulting gains and losses recognized as a component of corporate unallocated expense. These gains and losses are reflected in division results when the divisions take delivery of the underlying commodity. Therefore, division results reflect the contract purchase price of the energy or other commodities.

Division results are based on how our Chairman and Chief Executive Officer evaluates our divisions. Division results exclude certain Corporate-initiated restructuring and impairment charges, merger-related costs and divested businesses. For additional unaudited information on our divisions, see "Our Operations" in Management's Discussion and Analysis.

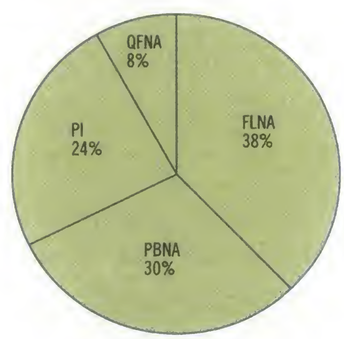


	2005	2004	2003	2005	2004	2003
	Net Revenue			Operating Profit		
FLNA	**$10,322**	$ 9,560	$ 9,091	**$2,529**	$2,389	$2,242
PBNA	**9,146**	8,313	7,733	**2,037**	1,911	1,690
PI	**11,376**	9,862	8,678	**1,607**	1,323	1,061
QFNA	**1,718**	1,526	1,467	**537**	475	470
Total division	**32,562**	29,261	26,969	**6,710**	6,098	5,463
Divested businesses	**–**	–	2	**–**	–	26
Corporate	**–**	–	–	**(788)**	(689)	(502)
	32,562	29,261	26,971	**5,922**	5,409	4,987
Restructuring and impairment charges	**–**	–	–	**–**	(150)	(147)
Merger-related costs	**–**	–	–	**–**	–	(59)
Total	**$32,562**	$29,261	$26,971	**$5,922**	$5,259	$4,781

Division Net Revenue



Division Operating Profit



Divested Businesses

During 2003, we sold our Quaker Foods North America Mission pasta business. The results of this business are reported as divested businesses.

Corporate

Corporate includes costs of our corporate headquarters, centrally managed initiatives, such as our BPT initiative, unallocated insurance and benefit programs, foreign exchange transaction gains and losses, and certain commodity derivative gains and losses, as well as profit-in-inventory elimination adjustments for our noncontrolled bottling affiliates and certain other items.

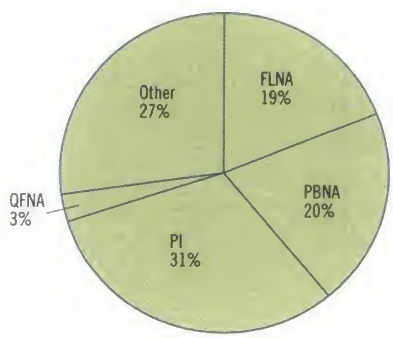
Restructuring and Impairment Charges and Merger-Related Costs — See Note 3.

Other Division Information

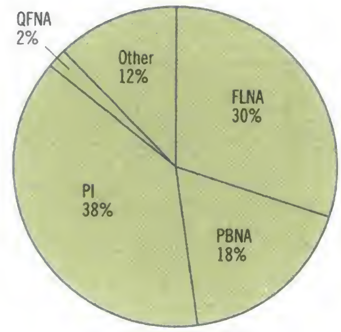
	2005	2004	2003	2005	2004	2003
	Total Assets			Capital Spending		
FLNA	$ 5,948	$ 5,476	$ 5,332	$ 512	$ 469	$ 426
PBNA	6,316	6,048	5,856	320	265	332
PI	9,983	8,921	8,109	667	537	521
QFNA	989	978	995	31	33	32
Total division	23,236	21,423	20,292	1,530	1,304	1,311
Corporate[(a)]	5,331	3,569	2,384	206	83	34
Investments in bottling affiliates	3,160	2,995	2,651	–	–	–
	$31,727	$27,987	$25,327	$1,736	$1,387	$1,345

(a) Corporate assets consist principally of cash and cash equivalents, short-term investments, and property, plant and equipment.

Total Assets



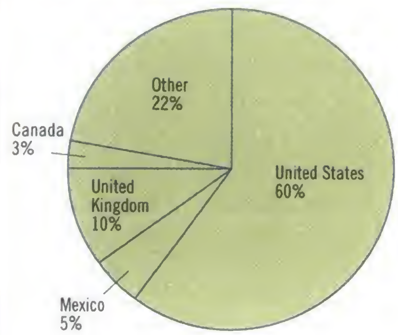
Capital Spending



Net Revenue

	2005	2004	2003	2005	2004	2003
	Amortization of Intangible Assets			Depreciation and Other Amortization		
FLNA	$ 3	$ 3	$ 3	$ 419	$ 420	$ 416
PBNA	76	75	75	264	258	245
PI	71	68	66	420	382	350
QFNA	–	1	1	34	36	36
Total division	150	147	145	1,137	1,096	1,047
Corporate	–	–	–	21	21	29
	$150	$147	$145	$1,158	$1,117	$1,076

Long-Lived Assets



	2005	2004	2003	2005	2004	2003
	Net Revenue[(a)]			Long-Lived Assets[(b)]		
U.S.	$19,937	$18,329	$17,377	$10,723	$10,212	$ 9,907
Mexico	3,095	2,724	2,642	902	878	869
United Kingdom	1,821	1,692	1,510	1,715	1,896	1,724
Canada	1,509	1,309	1,147	582	548	508
All other countries	6,200	5,207	4,295	3,948	3,339	3,123
	$32,562	$29,261	$26,971	$17,870	$16,873	$16,131

(a) Represents net revenue from businesses operating in these countries.

(b) Long-lived assets represent net property, plant and equipment, nonamortizable and net amortizable intangible assets and investments in noncontrolled affiliates. These assets are reported in the country where they are primarily used.

Note 2 — Our Significant Accounting Policies

Revenue Recognition

We recognize revenue upon shipment or delivery to our customers based on written sales terms that do not allow for a right of return. However, our policy for direct-store-delivery (DSD) and chilled products is to remove and replace damaged and out-of-date products from store shelves to ensure that our consumers receive the product quality and freshness that they expect. Similarly, our policy for warehouse distributed products is to replace damaged and out-of-date products. Based on our historical experience with this practice, we have reserved for anticipated damaged and out-of-date products. For additional unaudited information on our revenue recognition and related policies, including our policy on bad debts, see "Our Critical Accounting Policies" in Management's Discussion and Analysis. We are exposed to concentration of credit risk by our customers, Wal-Mart and PBG. Wal-Mart represents approximately 9% of our net revenue, including concentrate sales to our bottlers which are used in finished goods sold by them to Wal-Mart; and PBG represents approximately 10%. We have not experienced credit issues with these customers.

Sales Incentives and Other Marketplace Spending

We offer sales incentives and discounts through various programs to our customers and consumers. Sales incentives and discounts are accounted for as a reduction of revenue and totaled $8.9 billion in 2005, $7.8 billion in 2004 and $7.1 billion in 2003. While most of these incentive arrangements have terms of no more than one year, certain arrangements extend beyond one year. For example, fountain pouring rights may extend up to 15 years. Costs incurred to obtain these arrangements are recognized over the contract period and the remaining balances of $321 million at December 31, 2005 and $337 million at December 25, 2004 are included in current assets and other assets in our Consolidated Balance Sheet. For additional unaudited information on our sales incentives, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

Other marketplace spending includes the costs of advertising and other marketing activities and is reported as selling, general and administrative expenses. Advertising expenses were $1.8 billion in 2005, $1.7 billion in 2004 and $1.6 billion in 2003. Deferred advertising costs are not expensed until the year first used and consist of:

- media and personal service prepayments,
- promotional materials in inventory, and
- production costs of future media advertising.

Deferred advertising costs of $202 million and $137 million at year-end 2005 and 2004, respectively, are classified as prepaid expenses in our Consolidated Balance Sheet.

Distribution Costs

Distribution costs, including the costs of shipping and handling activities, are reported as selling, general and administrative expenses. Shipping and handling expenses were $4.1 billion in 2005, $3.9 billion in 2004 and $3.6 billion in 2003.

Cash Equivalents

Cash equivalents are investments with original maturities of three months or less which we do not intend to rollover beyond three months.

Software Costs

We capitalize certain computer software and software development costs incurred in connection with developing or obtaining computer software for internal use. Capitalized software costs are included in property, plant and equipment on our Consolidated Balance Sheet and amortized on a straight-line basis over the estimated useful lives of the software, which generally do not exceed 5 years. Net capitalized software and development costs were $327 million at December 31, 2005 and $181 million at December 25, 2004.

Commitments and Contingencies

We are subject to various claims and contingencies related to lawsuits, taxes and environmental matters, as well as commitments under contractual and other commercial obligations. We recognize liabilities for contingencies and commitments when a loss is probable and estimable. For additional information on our commitments, see Note 9.

Other Significant Accounting Policies

Our other significant accounting policies are disclosed as follows:

- *Property, Plant and Equipment and Intangible Assets* — Note 4 and, for additional unaudited information on brands and goodwill, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.
- *Income Taxes* — Note 5 and, for additional unaudited information, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.
- *Stock-Based Compensation Expense* — Note 6 and, for additional unaudited information, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.
- *Pension, Retiree Medical and Savings Plans* — Note 7 and, for additional unaudited information, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.
- *Risk Management* — Note 10 and, for additional unaudited information, see "Our Business Risks" in Management's Discussion and Analysis.

There have been no new accounting pronouncements issued or effective during 2005 that have had, or are expected to have, a material impact on our consolidated financial statements.

Note 3 — Restructuring and Impairment Charges and Merger-Related Costs

2005 Restructuring Charges

In the fourth quarter of 2005, we incurred a charge of $83 million ($55 million after-tax or $0.03 per share) in conjunction with actions taken to reduce costs in our operations, principally through headcount reductions. Of this charge, $34 million related to FLNA, $21 million to PBNA, $16 million to PI and $12 million to Corporate (recorded in corporate unallocated expenses). Most of this charge related to the termination of approximately 700 employees. We expect the substantial portion of the cash payments related to this charge to be paid in 2006.

2004 and 2003 Restructuring and Impairment Charges

In the fourth quarter of 2004, we incurred a charge of $150 million ($96 million after-tax or $0.06 per share) in conjunction with the consolidation of FLNA's manufacturing network as part of its ongoing productivity program. Of this charge, $93 million related to asset impairment, primarily reflecting the closure of four U.S. plants. Production from these plants was redeployed to other FLNA facilities in the U.S. The remaining $57 million included employee-related costs of $29 million, contract termination costs of $8 million and other exit costs of $20 million. Employee-related costs primarily reflect the termination costs for approximately 700 employees. Through December 31, 2005, we have paid $47 million and incurred non-cash charges of $10 million, leaving substantially no accrual.

In the fourth quarter of 2003, we incurred a charge of $147 million ($100 million after-tax or $0.06 per share) in conjunction with actions taken to streamline our North American divisions and PepsiCo International. These actions were taken to increase focus and eliminate redundancies at PBNA and PI and to improve the efficiency of the supply chain at FLNA. Of this charge, $81 million related to asset impairment, reflecting $57 million for the closure of a snack plant in Kentucky, the retirement of snack manufacturing lines in Maryland and Arkansas and $24 million for the closure of a PBNA office building in Florida. The remaining $66 million included employee-related costs of $54 million and facility and other exit costs of $12 million. Employee-related costs primarily reflect the termination costs for approximately 850 sales, distribution, manufacturing, research and marketing employees. As of December 31, 2005, all terminations had occurred and substantially no accrual remains.

Merger-Related Costs

In connection with the Quaker merger in 2001, we recognized merger-related costs of $59 million ($42 million after-tax or $0.02 per share) in 2003.

Note 4 — Property, Plant and Equipment and Intangible Assets

	Average Useful Life	2005	2004	2003
Property, plant and equipment, net				
Land and improvements	10 – 30 yrs.	$ 685	$ 646	
Buildings and improvements	20 – 44	3,736	3,605	
Machinery and equipment, including fleet and software	5 – 15	11,658	10,950	
Construction in progress		1,066	729	
		17,145	15,930	
Accumulated depreciation		(8,464)	(7,781)	
		$ 8,681	$ 8,149	
Depreciation expense		$1,103	$1,062	$1,020
Amortizable intangible assets, net				
Brands	5 – 40	$1,054	$1,008	
Other identifiable intangibles	3 – 15	257	225	
		1,311	1,233	
Accumulated amortization		(781)	(635)	
		$ 530	$ 598	
Amortization expense		$150	$147	$145

Depreciation and amortization are recognized on a straight-line basis over an asset's estimated useful life. Land is not depreciated and construction in progress is not depreciated until ready for service. Amortization of intangible assets for each of the next five years, based on average 2005 foreign exchange rates, is expected to be $152 million in 2006, $35 million in 2007, $35 million in 2008, $34 million in 2009 and $33 million in 2010.

Depreciable and amortizable assets are only evaluated for impairment upon a significant change in the operating or macroeconomic environment. In these circumstances, if an evaluation of the undiscounted cash flows indicates impairment, the asset is written down to its estimated fair value, which is based on discounted future cash flows. Useful lives are periodically evaluated to determine whether events or circumstances have occurred which indicate the need for revision. For additional unaudited information on our amortizable brand policies, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

Nonamortizable Intangible Assets

Perpetual brands and goodwill are assessed for impairment at least annually to ensure that discounted future cash flows continue to exceed the related book value. A perpetual brand is impaired if its book value exceeds its fair value. Goodwill is evaluated for impairment if the book value of its reporting unit exceeds its fair value. A reporting unit can be a division or business within a division. If the fair value of an evaluated asset is less than its book value, the asset is written down based on its discounted future cash flows to fair value. No impairment charges resulted from the required impairment evaluations. The change in the book value of nonamortizable intangible assets is as follows:

	Balance, Beginning 2004	Acquisition	Translation and Other	Balance, End of 2004	Acquisition	Translation and Other	Balance, End of 2005
Frito-Lay North America							
Goodwill	$ 130	$ –	$ 8	$ 138	$ –	$ 7	$ 145
PepsiCo Beverages North America							
Goodwill	2,157	–	4	2,161	–	3	2,164
Brands	59	–	–	59	–	–	59
	2,216	–	4	2,220	–	3	2,223
PepsiCo International							
Goodwill	1,334	29	72	1,435	278	(109)	1,604
Brands	808	–	61	869	263	(106)	1,026
	2,142	29	133	2,304	541	(215)	2,630
Quaker Foods North America							
Goodwill	175	–	–	175	–	–	175
Corporate							
Pension intangible	2	–	3	5	–	(4)	1
Total goodwill	3,796	29	84	3,909	278	(99)	4,088
Total brands	867	–	61	928	263	(106)	1,085
Total pension intangible	2	–	3	5	–	(4)	1
	$4,665	$29	$148	$4,842	$541	$(209)	$5,174

Note 5 — Income Taxes

	2005	2004	2003
Income before income taxes — continuing operations			
U.S.	$3,175	$2,946	$3,267
Foreign	3,207	2,600	1,725
	$6,382	$5,546	$4,992
Provision for income taxes — continuing operations			
Current: U.S. Federal	$1,638	$1,030	$1,326
Foreign	426	256	341
State	118	69	80
	2,182	1,355	1,747
Deferred: U.S. Federal	137	11	(274)
Foreign	(26)	5	(47)
State	11	1	(2)
	122	17	(323)
	$2,304	$1,372	$1,424
Tax rate reconciliation — continuing operations			
U.S. Federal statutory tax rate	35.0%	35.0%	35.0%
State income tax, net of U.S. Federal tax benefit	1.4	0.8	1.0
Taxes on AJCA repatriation	7.0	–	–
Lower taxes on foreign results	(6.5)	(5.4)	(5.5)
Settlement of prior years' audit	–	(4.8)	(2.2)
Other, net	(0.8)	(0.9)	0.2
Annual tax rate	36.1%	24.7%	28.5%
Deferred tax liabilities			
Investments in noncontrolled affiliates	$ 993	$ 850	
Property, plant and equipment	772	857	
Pension benefits	863	669	
Intangible assets other than nondeductible goodwill	135	153	
Zero coupon notes	35	46	
Other	169	157	
Gross deferred tax liabilities	2,967	2,732	
Deferred tax assets			
Net carryforwards	608	666	
Stock-based compensation	426	402	
Retiree medical benefits	400	402	
Other employee-related benefits	342	379	
Other	520	460	
Gross deferred tax assets	2,296	2,309	
Valuation allowances	(532)	(564)	
Deferred tax assets, net	1,764	1,745	
Net deferred tax liabilities	$1,203	$ 987	
Deferred taxes included within:			
Prepaid expenses and other current assets	$231	$229	
Deferred income taxes	$1,434	$1,216	
Analysis of valuation allowances			
Balance, beginning of year	$564	$438	$487
(Benefit)/provision	(28)	118	(52)
Other (deductions)/additions	(4)	8	3
Balance, end of year	$532	$564	$438

For additional unaudited information on our income tax policies, including our reserves for income taxes, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

Carryforwards, Credits and Allowances

Operating loss carryforwards totaling $5.1 billion at year-end 2005 are being carried forward in a number of foreign and state jurisdictions where we are permitted to use tax operating losses from prior periods to reduce future taxable income. These operating losses will expire as follows: $0.1 billion in 2006, $4.1 billion between 2007 and 2025 and $0.9 billion may be carried forward indefinitely. In addition, certain tax credits generated in prior periods of approximately $39.4 million are available to reduce certain foreign tax liabilities through 2011. We establish valuation allowances for our deferred tax assets when the amount of expected future taxable income is not likely to support the use of the deduction or credit.

Undistributed International Earnings

The AJCA created a one-time incentive for U.S. corporations to repatriate undistributed international earnings by providing an 85% dividends received deduction. As approved by our Board of Directors in July 2005, we repatriated approximately $7.5 billion in earnings previously considered indefinitely reinvested outside the U.S. in the fourth quarter of 2005. In 2005, we recorded income tax expense of $460 million associated with this repatriation. Other than the earnings repatriated, we intend to continue to reinvest earnings outside the U.S. for the foreseeable future and, therefore, have not recognized any U.S. tax expense on these earnings. At December 31, 2005, we had approximately $7.5 billion of undistributed international earnings.

Reserves

A number of years may elapse before a particular matter, for which we have established a reserve, is audited and finally resolved. The number of years with open tax audits varies depending on the tax jurisdiction. During 2004, we recognized $266 million of tax benefits related to the favorable resolution of certain open tax issues. In addition, in 2004, we recognized a tax benefit of $38 million upon agreement with the IRS on an open issue related to our discontinued restaurant operations. At the end of 2003, we entered into agreements with the IRS for open years through 1997. These agreements resulted in a tax benefit of $109 million in the fourth quarter of 2003. As part of these agreements, we also resolved the treatment of certain other issues related to future tax years.

The IRS has initiated their audits of our tax returns for the years 1998 through 2002. Our tax returns subsequent to 2002 have not yet been examined. While it is often difficult to predict the final outcome or the timing of resolution of any particular tax matter, we believe that our reserves reflect the probable outcome of known tax contingencies. Settlement of any particular issue would usually require the use of cash. Favorable resolution would be recognized as a reduction to our annual tax rate in the year of resolution. Our tax reserves, covering all federal, state and foreign jurisdictions, are presented in the balance sheet within other liabilities (see Note 14), except for any amounts relating to items we expect to pay in the coming year which are included in current income taxes payable. For further unaudited information on the impact of the resolution of open tax issues, see "Other Consolidated Results."

Note 6 — Stock-Based Compensation

Our stock-based compensation program is a broad-based program designed to attract and retain employees while also aligning employees' interests with the interests of our shareholders. Employees at all levels participate in our stock-based compensation program. In addition, members of our Board of Directors participate in our stock-based compensation program in connection with their service on our Board. Stock options and RSUs are granted to employees under the shareholder-approved 2003 Long-Term Incentive Plan (LTIP), our only active stock-based plan. Stock-based compensation expense was $311 million in 2005, $368 million in 2004 and $407 million in 2003. Related income tax benefits recognized in earnings were $87 million in 2005, $103 million in 2004 and $114 million in 2003. At year-end 2005, 51 million shares were available for future executive and SharePower grants. For additional unaudited information on our stock-based compensation program, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

SharePower Grants

SharePower options are awarded under our LTIP to all eligible employees, based on job level or classification, and in the case of international employees, tenure as well. All stock option grants have an exercise price equal to the fair market value of our common stock on the day of grant and generally have a 10-year term with vesting after three years.

Executive Grants

All senior management and certain middle management are eligible for executive grants under our LTIP. All stock option grants have an exercise price equal to the fair market value of our common stock on the day of grant and generally have a 10-year term with vesting after three years. There have been no reductions to the exercise price of previously issued awards, and any repricing of awards would require approval of our shareholders.

Beginning in 2004, executives who are awarded long-term incentives based on their performance are offered the choice of stock options or RSUs. RSU expense is based on the fair value of PepsiCo stock on the date of grant and is amortized over the vesting period, generally three years. Each restricted stock unit can be settled in a share of our stock after the vesting period. Executives who elect RSUs receive one RSU for every four stock options that would have otherwise been granted. Senior officers do not have a choice and are granted 50% stock options and 50% RSUs. Vesting of RSU awards for senior officers is contingent upon the achievement of pre-established performance targets. We granted 3 million RSUs in both 2005 and 2004 with weighted-average intrinsic values of $53.83 and $47.28, respectively.

Method of Accounting and Our Assumptions

We account for our employee stock options under the fair value method of accounting using a Black-Scholes valuation model to measure stock-based compensation expense at the date of grant. We adopted SFAS 123R, *Share-Based Payment*, under the modified prospective method in the first quarter of 2006. We do not expect our adoption of SFAS 123R to materially impact our financial statements.

Our weighted-average Black-Scholes fair value assumptions include:

	2005	2004	2003
Expected life	6 yrs.	6 yrs.	6 yrs.
Risk free interest rate	3.8%	3.3%	3.1%
Expected volatility	23%	26%	27%
Expected dividend yield	1.8%	1.8%	1.15%

Our Stock Option Activity[a]

	2005		2004		2003	
	Options	Average Price[b]	Options	Average Price[b]	Options	Average Price[b]
Outstanding at beginning of year	174,261	$40.05	198,173	$38.12	190,432	$36.45
Granted	12,328	53.82	14,137	47.47	41,630	39.89
Exercised	(30,945)	35.40	(31,614)	30.57	(25,833)	26.74
Forfeited/expired	(5,495)	43.31	(6,435)	43.82	(8,056)	43.56
Outstanding at end of year	150,149	42.03	174,261	40.05	198,173	38.12
Exercisable at end of year	89,652	40.52	94,643	36.41	97,663	32.56

Stock options outstanding and exercisable at December 31, 2005[a]

	Options Outstanding			Options Exercisable		
Range of Exercise Price	Options	Average Price[b]	Average Life[c]	Options	Average Price[b]	Average Life[c]
$14.40 to $21.54	905	$20.01	3.56 yrs.	905	$20.01	3.56 yrs.
$23.00 to $33.75	14,559	30.46	3.07	14,398	30.50	3.05
$34.00 to $43.50	82,410	39.44	5.34	48,921	39.19	4.10
$43.75 to $56.75	52,275	49.77	7.17	25,428	49.48	6.09
	150,149	42.03	5.67	89,652	40.52	4.45

(a) Options are in thousands and include options previously granted under Quaker plans. No additional options or shares may be granted under the Quaker plans.

(b) Weighted-average exercise price.

(c) Weighted-average contractual life remaining.

Our RSU Activity[a]

	2005			2004		
	RSUs	Average Intrinsic Value[b]	Average Life[c]	RSUs	Average Intrinsic Value[b]	Average Life[c]
Outstanding at beginning of year	2,922	$47.30		–	$ –	
Granted	3,097	53.83		3,077	47.28	
Converted	(91)	48.73		(18)	47.25	
Forfeited/expired	(259)	50.51		(137)	47.25	
Outstanding at end of year	5,669	50.70	1.8 yrs.	2,922	47.30	2.2 yrs.

(a) RSUs are in thousands.

(b) Weighted-average intrinsic value.

(c) Weighted-average contractual life remaining.

Other stock-based compensation data

	Stock Options			RSUs	
	2005	2004	2003	2005	2004
Weighted-average fair value of options granted	$13.45	$12.04	$11.21		
Total intrinsic value of options/RSUs exercised/converted[a]	$632,603	$667,001	$466,719	$4,974	$914
Total intrinsic value of options/RSUs outstanding[a]	$2,553,594	$2,062,153	$1,641,505	$334,931	$151,760
Total intrinsic value of options exercisable[a]	$1,662,198	$1,464,926	$1,348,658		

(a) In thousands.

At December 31, 2005, there was $315 million of total unrecognized compensation cost related to nonvested share-based compensation grants. This unrecognized compensation is expected to be recognized over a weighted-average period of 1.6 years.

Note 7 — Pension, Retiree Medical and Savings Plans

Our pension plans cover full-time employees in the U.S. and certain international employees. Benefits are determined based on either years of service or a combination of years of service and earnings. U.S. retirees are also eligible for medical and life insurance benefits (retiree medical) if they meet age and service requirements. Generally, our share of retiree medical costs is capped at specified dollar amounts, which vary based upon years of service, with retirees contributing the remainder of the costs. We use a September 30 measurement date and all plan assets and liabilities are generally reported as of that date. The cost or benefit of plan changes that increase or decrease benefits for prior employee service (prior service cost) is included in expense on a straight-line basis over the average remaining service period of employees expected to receive benefits.

The Medicare Act was signed into law in December 2003 and we applied the provisions of the Medicare Act to our plans in 2005 and 2004. The Medicare Act provides a subsidy for sponsors of retiree medical plans who offer drug benefits equivalent to those provided under Medicare. As a result of the Medicare Act, our 2005 and 2004 retiree medical costs were $11 million and $7 million lower, respectively, and our 2005 and 2004 liabilities were reduced by $136 million and $80 million, respectively. We expect our 2006 retiree medical costs to be approximately $18 million lower than they otherwise would have been as a result of the Medicare Act.

For additional unaudited information on our pension and retiree medical plans and related accounting policies and assumptions, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

	Pension						Retiree Medical		
	U.S.			International					
	2005	2004	2003	**2005**	2004	2003	**2005**	2004	2003
Weighted-average assumptions									
Liability discount rate	**5.7%**	6.1%	6.1%	**5.1%**	6.1%	6.1%	**5.7%**	6.1%	6.1%
Expense discount rate	**6.1%**	6.1%	6.7%	**6.1%**	6.1%	6.4%	**6.1%**	6.1%	6.7%
Expected return on plan assets	**7.8%**	7.8%	8.3%	**8.0%**	8.0%	8.0%	**–**	–	–
Rate of compensation increases	**4.4%**	4.5%	4.5%	**4.1%**	3.9%	3.8%	**–**	–	–
Components of benefit expense									
Service cost	**$ 213**	$ 193	$ 153	**$ 32**	$ 27	$ 24	**$ 40**	$ 38	$ 33
Interest cost	**296**	271	245	**55**	47	39	**78**	72	73
Expected return on plan assets	**(344)**	(325)	(305)	**(69)**	(65)	(54)	**–**	–	–
Amortization of prior service cost/(benefit)	**3**	6	6	**1**	1	–	**(11)**	(8)	(3)
Amortization of experience loss	**106**	81	44	**15**	9	5	**26**	19	13
Benefit expense	**274**	226	143	**34**	19	14	**133**	121	116
Settlement/curtailment loss	**–**	4	–	**–**	1	–	**–**	–	–
Special termination benefits	**21**	19	4	**–**	1	–	**2**	4	–
Total	**$ 295**	$ 249	$ 147	**$ 34**	$ 21	$ 14	**$135**	$125	$116

	Pension				Retiree Medical	
	2005	2004	2005	2004	2005	2004
	U.S.		International			
Change in projected benefit liability						
Liability at beginning of year	$4,968	$4,456	$ 952	$758	$1,319	$1,264
Service cost	213	193	32	27	40	38
Interest cost	296	271	55	47	78	72
Plan amendments	–	(17)	3	1	(8)	(41)
Participant contributions	–	–	10	9	–	–
Experience loss/(gain)	517	261	203	73	(45)	58
Benefit payments	(241)	(205)	(28)	(29)	(74)	(76)
Settlement/curtailment loss	–	(9)	–	(2)	–	–
Special termination benefits	21	18	–	1	2	4
Foreign currency adjustment	–	–	(68)	67	–	–
Other	(3)	–	104	–	–	–
Liability at end of year	$5,771	$4,968	$1,263	$952	$1,312	$1,319
Liability at end of year for service to date	$4,783	$4,164	$1,047	$779		
Change in fair value of plan assets						
Fair value at beginning of year	$4,152	$3,558	$ 838	$687	$ –	$ –
Actual return on plan assets	477	392	142	77	–	–
Employer contributions/funding	699	416	104	37	74	76
Participant contributions	–	–	10	9	–	–
Benefit payments	(241)	(205)	(28)	(29)	(74)	(76)
Settlement/curtailment loss	–	(9)	–	(2)	–	–
Foreign currency adjustment	–	–	(61)	59	–	–
Other	(1)	–	94	–	–	–
Fair value at end of year	$5,086	$4,152	$1,099	$838	$ –	$ –
Funded status as recognized in our Consolidated Balance Sheet						
Funded status at end of year	$ (685)	$ (817)	$(164)	$(113)	$(1,312)	$(1,319)
Unrecognized prior service cost/(benefit)	5	9	17	13	(113)	(116)
Unrecognized experience loss	2,288	2,013	474	380	402	473
Fourth quarter benefit payments	5	5	4	7	19	19
Net amounts recognized	$1,613	$1,210	$ 331	$ 287	$(1,004)	$ (943)
Net amounts as recognized in our Consolidated Balance Sheet						
Other assets	$2,068	$1,572	$367	$294	$ –	$ –
Intangible assets	–	–	1	5	–	–
Other liabilities	(479)	(387)	(41)	(37)	(1,004)	(943)
Accumulated other comprehensive loss	24	25	4	25	–	–
Net amounts recognized	$1,613	$1,210	$331	$287	$(1,004)	$(943)
Components of increase in unrecognized experience loss						
Decrease in discount rate	$ 365	$ –	$194	$ 4	$ 61	$ –
Employee-related assumption changes	57	196	2	65	–	109
Liability-related experience different from assumptions	95	65	7	4	(54)	31
Actual asset return different from expected return	(133)	(67)	(73)	(12)	–	–
Amortization of losses	(106)	(81)	(15)	(9)	(26)	(19)
Other, including foreign currency adjustments and 2003 Medicare Act	(3)	(5)	(22)	26	(52)	(82)
Total	$ 275	$108	$ 93	$ 78	$(71)	$ 39
Selected information for plans with liability for service to date in excess of plan assets						
Liability for service to date	$(374)	$(320)	$(65)	$(191)	$(1,312)	$(1,319)
Projected benefit liability	$(815)	$(685)	$(84)	$(227)	$(1,312)	$(1,319)
Fair value of plan assets	$8	$11	$33	$161	$–	$–

Of the total projected pension benefit liability at year-end 2005, $765 million relates to plans that we do not fund because the funding of such plans does not receive favorable tax treatment.

Future Benefit Payments

Our estimated future benefit payments are as follows:

	2006	2007	2008	2009	2010	2011-15
Pension	$235	$255	$275	$300	$330	$2,215
Retiree medical	$85	$90	$90	$95	$100	$545

These future benefits to beneficiaries include payments from both funded and unfunded pension plans.

Pension Assets

The expected return on pension plan assets is based on our historical experience, our pension plan investment guidelines, and our expectations for long-term rates of return. We use a market-related value method that recognizes each year's asset gain or loss over a five-year period. Therefore, it takes five years for the gain or loss from any one year to be fully included in the value of pension plan assets that is used to calculate the expected return. Our pension plan investment guidelines are established based upon an evaluation of market conditions, tolerance for risk and cash requirements for benefit payments. Our investment objective is to ensure that funds are available to meet the plans' benefit obligations when they are due. Our investment strategy is to prudently invest plan assets in high-quality and diversified equity and debt securities to achieve our long-term return expectation. Our target allocation and actual pension plan asset allocations for the plan years 2005 and 2004, are below.

Pension assets include approximately 5.5 million shares of PepsiCo common stock with a market value of $311 million in 2005, and 5.5 million shares with a market value of $267 million in 2004. Our investment policy limits the investment in PepsiCo stock at the time of investment to 10% of the fair value of plan assets.

		Actual Allocation	
Asset Category	Target Allocation	2005	2004
Equity securities	60%	**60%**	60%
Debt securities	40%	**39%**	39%
Other, primarily cash	–	**1%**	1%
Total	100%	**100%**	100%

Retiree Medical Cost Trend Rates

An average increase of 10% in the cost of covered retiree medical benefits is assumed for 2006. This average increase is then projected to decline gradually to 5% in 2010 and thereafter. These assumed health care cost trend rates have an impact on the retiree medical plan expense and liability. However, the cap on our share of retiree medical costs limits the impact. A 1 percentage point change in the assumed health care trend rate would have the following effects:

	1% Increase	1% Decrease
2005 service and interest cost components	$3	$(2)
2005 benefit liability	$38	$(33)

Savings Plans

Our U.S. employees are eligible to participate in 401(k) savings plans, which are voluntary defined contribution plans. The plans are designed to help employees accumulate additional savings for retirement. We make matching contributions on a portion of eligible pay based on years of service. In 2005 and 2004, our matching contributions were $52 million and $35 million, respectively.

Note 8 — Noncontrolled Bottling Affiliates

Our most significant noncontrolled bottling affiliates are PBG and PAS. Approximately 10% of our net revenue in 2005, 2004 and 2003 reflects sales to PBG.

The Pepsi Bottling Group

In addition to approximately 41% and 42% of PBG's outstanding common stock that we own at year-end 2005 and 2004, respectively, we own 100% of PBG's class B common stock and approximately 7% of the equity of Bottling Group, LLC, PBG's principal operating subsidiary. This gives us economic ownership of approximately 45% and 46% of PBG's combined operations at year-end 2005 and 2004, respectively. In 2005, bottling equity income includes $126 million of pre-tax gains on our sales of PBG stock.

PBG's summarized financial information is as follows:

	2005	2004	2003
Current assets	$ 2,412	$ 2,183	
Noncurrent assets	9,112	8,754	
Total assets	$11,524	$10,937	
Current liabilities	$2,598	$1,725	
Noncurrent liabilities	6,387	6,818	
Minority interest	496	445	
Total liabilities	$9,481	$8,988	
Our investment	$1,738	$1,594	
Net revenue	$11,885	$10,906	$10,265
Gross profit	$5,632	$5,250	$5,050
Operating profit	$1,023	$976	$956
Net income	$466	$457	$416

Our investment in PBG, which includes the related goodwill, was $400 million and $321 million higher than our ownership interest in their net assets at year-end 2005 and 2004, respectively. Based upon the quoted closing price of PBG shares at year-end 2005 and 2004, the calculated market value of our shares in PBG, excluding our investment in Bottling Group, LLC, exceeded our investment balance by approximately $1.5 billion and $1.7 billion, respectively.

PepsiAmericas

At year-end 2005 and 2004, we owned approximately 43% and 41% of PepsiAmericas, respectively, and their summarized financial information is as follows:

	2005	2004	2003
Current assets	$ 598	$ 530	
Noncurrent assets	3,456	3,000	
Total assets	$4,054	$3,530	
Current liabilities	$ 722	$ 521	
Noncurrent liabilities	1,763	1,386	
Total liabilities	$2,485	$1,907	
Our investment	$968	$924	
Net revenue	$3,726	$3,345	$3,237
Gross profit	$1,562	$1,423	$1,360
Operating profit	$393	$340	$316
Net income	$195	$182	$158

Our investment in PAS, which includes the related goodwill, was $292 million and $253 million higher than our ownership interest in their net assets at year-end 2005 and 2004, respectively. Based upon the quoted closing price of PAS shares at year-end 2005 and 2004, the calculated market value of our shares in PepsiAmericas exceeded our investment balance by approximately $364 million and $277 million, respectively.

In January 2005, PAS acquired a regional bottler, Central Investment Corporation. The table above includes the results of Central Investment Corporation from the transaction date forward.

Related Party Transactions

Our significant related party transactions involve our noncontrolled bottling affiliates. We sell concentrate to these affiliates, which is used in the production of carbonated soft drinks and non-carbonated beverages. We also sell certain finished goods to these affiliates and we receive royalties for the use of our trademarks for certain products. Sales of concentrate and finished goods are reported net of bottler funding. For further unaudited information on these bottlers, see "Our Customers" in Management's Discussion and Analysis. These transactions with our bottling affiliates are reflected in our consolidated financial statements as follows:

	2005	2004	2003
Net revenue	$4,633	$4,170	$3,699
Selling, general and administrative expenses	$143	$114	$128
Accounts and notes receivable	$178	$157	
Accounts payable and other current liabilities	$117	$95	

Such amounts are settled on terms consistent with other trade receivables and payables. See Note 9 regarding our guarantee of certain PBG debt.

In addition, we coordinate, on an aggregate basis, the negotiation and purchase of sweeteners and other raw materials requirements for certain of our bottlers with suppliers. Once we have negotiated the contracts, the bottlers order and take delivery directly from the supplier and pay the suppliers directly. Consequently, these transactions are not reflected in our consolidated financial statements. As the contracting party, we could be liable to these suppliers in the event of any nonpayment by our bottlers, but we consider this exposure to be remote.

Note 9 — Debt Obligations and Commitments

	2005	2004
Short-term debt obligations		
Current maturities of long-term debt	$ 143	$ 160
Commercial paper (3.3% and 1.6%)	3,140	1,287
Other borrowings (7.4% and 6.6%)	356	357
Amounts reclassified to long-term debt	(750)	(750)
	$2,889	$1,054
Long-term debt obligations		
Short-term borrowings, reclassified	$ 750	$ 750
Notes due 2006-2026 (5.4% and 4.7%)	1,161	1,274
Zero coupon notes, $475 million due 2006-2012 (13.4%)	312	321
Other, due 2006-2014 (6.3% and 6.2%)	233	212
	2,456	2,557
Less: current maturities of long-term debt obligations	(143)	(160)
	$2,313	$2,397

The interest rates in the above table reflect weighted-average rates as of year-end.

Short-term borrowings are reclassified to long-term when we have the intent and ability, through the existence of the unused lines of credit, to refinance these borrowings on a long-term basis. At year-end 2005, we maintained $2.1 billion in corporate lines of credit subject to normal banking terms and conditions. These credit facilities support short-term debt issuances and remained unused as of December 31, 2005. Of the $2.1 billion, $1.35 billion expires in May 2006 with the remaining $750 million expiring in June 2009.

In addition, $181 million of our debt was outstanding on various lines of credit maintained for our international divisions. These lines of credit are subject to normal banking terms and conditions and are committed to the extent of our borrowings.

Interest Rate Swaps

We entered into interest rate swaps in 2004 to effectively convert the interest rate of a specific debt issuance from a fixed rate of 3.2% to a variable rate. The variable weighted-average interest rate that we pay is linked to LIBOR and is subject to change. The notional amount of the interest rate swaps outstanding at December 31, 2005 and December 25, 2004 was $500 million. The terms of the interest rate swaps match the terms of the debt they modify. The swaps mature in 2007.

At December 31, 2005, approximately 78% of total debt, after the impact of the associated interest rate swaps, was exposed to variable interest rates, compared to 67% at December 25, 2004. In addition to variable rate long-term debt, all debt with maturities of less than one year is categorized as variable for purposes of this measure.

Cross Currency Interest Rate Swaps

In 2004, we entered into a cross currency interest rate swap to hedge the currency exposure on U.S. dollar denominated debt of $50 million held by a foreign affiliate. The terms of this swap match the terms of the debt it modifies. The swap matures in 2008. The unrecognized gain related to this swap was less than $1 million at December 31, 2005, resulting in a U.S. dollar liability of $50 million. At December 25, 2004, the unrecognized loss related to this swap was $3 million, resulting in a U.S. dollar liability of $53 million. We have also entered into cross currency interest rate swaps to hedge the currency exposure on U.S. dollar denominated intercompany debt of $125 million. The terms of the swaps match the terms of the debt they modify. The swaps mature over the next two years. The net unrecognized gain related to these swaps was $5 million at December 31, 2005. The net unrecognized loss related to these swaps was less than $1 million at December 25, 2004.

Long-Term Contractual Commitments

Payments Due by Period	Total	2006	2007-2008	2009-2010	2011 and beyond
Long-term debt obligations[(a)]	$2,313	$ –	$1,052	$ 876	$ 385
Operating leases	769	187	253	132	197
Purchasing commitments[(b)]	4,533	1,169	1,630	775	959
Marketing commitments	1,487	412	438	381	256
Other commitments	99	82	10	6	1
	$9,201	$1,850	$3,383	$2,170	$1,798

(a) Excludes current maturities of long-term debt of $143 million which are classified within current liabilities.

(b) Includes approximately $13 million of long-term commitments which are reflected in other liabilities in our Consolidated Balance Sheet.

The above table reflects non-cancelable commitments as of December 31, 2005 based on year-end foreign exchange rates.

Most long-term contractual commitments, except for our long-term debt obligations, are not recorded in our Consolidated Balance Sheet. Non-cancelable operating leases primarily represent building leases. Non-cancelable purchasing commitments are primarily for oranges and orange juices to be used for our Tropicana brand beverages. Non-cancelable marketing commitments primarily are for sports marketing and with our fountain customers. Bottler funding is not reflected in our long-term contractual commitments as it is negotiated on an annual basis. See Note 7 regarding our pension and retiree medical obligations and discussion below regarding our commitments to noncontrolled bottling affiliates and former restaurant operations.

Off-Balance Sheet Arrangements

It is not our business practice to enter into off-balance sheet arrangements, other than in the normal course of business, nor is it our policy to issue guarantees to our bottlers, noncontrolled affiliates or third parties. However, certain guarantees were necessary to facilitate the separation of our bottling and restaurant operations from us. In connection with these transactions, we have guaranteed $2.3 billion of Bottling Group, LLC's long-term debt through 2012 and $28 million of YUM! Brands, Inc. (YUM) outstanding obligations, primarily property leases, through 2020. The terms of our Bottling Group, LLC debt guarantee are intended to preserve the structure of PBG's separation from us and our payment obligation would be triggered if Bottling Group, LLC failed to perform under these debt obligations or the structure significantly changed. Our guarantees of certain obligations ensured YUM's continued use of certain properties. These guarantees would require our cash payment if YUM failed to perform under these lease obligations.

See "Our Liquidity, Capital Resources and Financial Position" in Management's Discussion and Analysis for further unaudited information on our borrowings.

Note 10 — Risk Management

We are exposed to the risk of loss arising from adverse changes in:

- commodity prices, affecting the cost of our raw materials and energy,
- foreign exchange risks,
- interest rates,
- stock prices, and
- discount rates affecting the measurement of our pension and retiree medical liabilities.

In the normal course of business, we manage these risks through a variety of strategies, including the use of derivatives. Certain derivatives are designated as either cash flow or fair value hedges and qualify for hedge accounting treatment, while others do not qualify and are marked to market through earnings. See "Our Business Risks" in Management's Discussion and Analysis for further unaudited information on our business risks.

For cash flow hedges, changes in fair value are deferred in accumulated other comprehensive loss within shareholders' equity until the underlying hedged item is recognized in net income. For fair value hedges, changes in fair value are recognized immediately in earnings, consistent with the underlying hedged item. Hedging transactions are limited to an underlying exposure. As a result, any change in the value of our derivative instruments would be substantially offset by an opposite change in the value of the underlying hedged items. Hedging ineffectiveness and a net earnings impact occur when the change in the value of the hedge does not offset the change in the value of the underlying hedged item. If the derivative instrument is terminated, we continue to defer the related gain or loss and include it as a component of the cost of the underlying hedged item. Upon determination that the underlying hedged item will not be part of an actual transaction, we recognize the related gain or loss in net income in that period.

We also use derivatives that do not qualify for hedge accounting treatment. We account for such derivatives at market value with the resulting gains and losses reflected in our income statement. We do not use derivative instruments for trading or speculative purposes and we limit our exposure to individual counterparties to manage credit risk.

Commodity Prices

We are subject to commodity price risk because our ability to recover increased costs through higher pricing may be limited in the competitive environment in which we operate. This risk is managed through the use of fixed-price purchase orders, pricing agreements, geographic diversity and derivatives. We use derivatives, with terms of no more than two years, to economically hedge price fluctuations related to a portion of our anticipated commodity purchases, primarily for natural gas and diesel fuel. For those derivatives that are designated as cash flow hedges, any ineffectiveness is recorded immediately. However, our commodity cash flow hedges have not had any significant ineffectiveness for all periods presented. We classify both the earnings and cash flow impact from these derivatives consistent with the underlying hedged item. During the next 12 months, we expect to reclassify gains of $24 million related to cash flow hedges from accumulated other comprehensive loss into net income.

Foreign Exchange

Our operations outside of the U.S. generate over a third of our net revenue of which Mexico, the United Kingdom and Canada comprise nearly 20%. As a result, we are exposed to foreign currency risks from unforeseen economic changes and political unrest. On occasion, we enter into hedges, primarily forward contracts with terms of no more than two years, to reduce the effect of foreign exchange rates. Ineffectiveness on these hedges has not been material.

Interest Rates

We centrally manage our debt and investment portfolios considering investment opportunities and risks, tax consequences and overall financing strategies. We may use interest rate and cross currency interest rate swaps to manage our overall interest expense and foreign exchange risk. These instruments effectively change the interest rate and currency of specific debt issuances. These swaps are entered into

concurrently with the issuance of the debt that they are intended to modify. The notional amount, interest payment and maturity date of the swaps match the principal, interest payment and maturity date of the related debt. These swaps are entered into only with strong creditworthy counterparties, are settled on a net basis and are of relatively short duration.

Stock Prices

The portion of our deferred compensation liability that is based on certain market indices and on our stock price is subject to market risk. We hold mutual fund investments and prepaid forward contracts to manage this risk. Changes in the fair value of these investments and contracts are recognized immediately in earnings and are offset by changes in the related compensation liability.

Fair Value

All derivative instruments are recognized in our Consolidated Balance Sheet at fair value. The fair value of our derivative instruments is generally based on quoted market prices. Book and fair values of our derivative and financial instruments are as follows:

	2005		2004	
	Book Value	**Fair Value**	Book Value	Fair Value
Assets				
Cash and cash equivalents(a)	**$1,716**	**$1,716**	$1,280	$1,280
Short-term investments(b)	**$3,166**	**$3,166**	$2,165	$2,165
Forward exchange contracts(c)	**$19**	**$19**	$8	$8
Commodity contracts(d)	**$41**	**$41**	$7	$7
Prepaid forward contract(e)	**$107**	**$107**	$120	$120
Cross currency interest rate swaps(f)	**$6**	**$6**	$–	$–
Liabilities				
Forward exchange contracts(c)	**$15**	**$15**	$35	$35
Commodity contracts(d)	**$3**	**$3**	$8	$8
Debt obligations	**$5,202**	**$5,378**	$3,451	$3,676
Interest rate swaps(g)	**$9**	**$9**	$1	$1
Cross currency interest rate swaps(f)	**$–**	**$–**	$3	$3

Included in our Consolidated Balance Sheet under the captions noted above or as indicated below. In addition, derivatives are designated as accounting hedges unless otherwise noted below.

(a) Book value approximates fair value due to the short maturity.

(b) Principally short-term time deposits and includes $124 million at December 31, 2005 and $118 million at December 25, 2004 of mutual fund investments used to manage a portion of market risk arising from our deferred compensation liability.

(c) 2005 asset includes $14 million related to derivatives not designated as accounting hedges. Assets are reported within current assets and other assets and liabilities are reported within current liabilities and other liabilities.

(d) 2005 asset includes $2 million related to derivatives not designated as accounting hedges and the liability relates entirely to derivatives not designated as accounting hedges. Assets are reported within current assets and other assets and liabilities are reported within current liabilities and other liabilities.

(e) Included in current assets and other assets.

(f) Asset included within other assets and liability included in long-term debt.

(g) Reported in other liabilities.

This table excludes guarantees, including our guarantee of $2.3 billion of Bottling Group, LLC's long-term debt. The guarantee had a fair value of $47 million at December 31, 2005 and $46 million at December 25, 2004 based on an external estimate of the cost to us of transferring the liability to an independent financial institution. See Note 9 for additional information on our guarantees.

Note 11 — Net Income per Common Share from Continuing Operations

Basic net income per common share is net income available to common shareholders divided by the weighted average of common shares outstanding during the period. Diluted net income per common share is calculated using the weighted average of common shares outstanding adjusted to include the effect that would occur if in-the-money employee stock options were exercised and RSUs and preferred shares were converted into common shares. Options to purchase 3.0 million shares in 2005, 7.0 million shares in 2004 and 49.0 million shares in 2003 were not included in the calculation of diluted earnings per common share because these options were out-of-the-money. Out-of-the-money options had average exercise prices of $53.77 in 2005, $52.88 in 2004 and $48.27 in 2003.

The computations of basic and diluted net income per common share from continuing operations are as follows:

	2005 Income	2005 Shares(a)	2004 Income	2004 Shares(a)	2003 Income	2003 Shares(a)
Net income	$4,078		$4,174		$3,568	
Preferred shares:						
Dividends	(2)		(3)		(3)	
Redemption premium	(16)		(22)		(12)	
Net income available for common shareholders	$4,060	1,669	$4,149	1,696	$3,553	1,718
Basic net income per common share	$2.43		$2.45		$2.07	
Net income available for common shareholders	$4,060	1,669	$4,149	1,696	$3,553	1,718
Dilutive securities:						
Stock options and RSUs	–	35	–	31	–	17
ESOP convertible preferred stock	18	2	24	2	15	3
Unvested stock awards	–	–	–	–	–	1
Diluted	$4,078	1,706	$4,173	1,729	$3,568	1,739
Diluted net income per common share	$2.39		$2.41		$2.05	

(a) Weighted-average common shares outstanding.

Note 12 — Preferred and Common Stock

As of December 31, 2005 and December 25, 2004, there were 3.6 billion shares of common stock and 3 million shares of convertible preferred stock authorized. The preferred stock was issued only for an employee stock ownership plan (ESOP) established by Quaker and these shares are redeemable for common stock by the ESOP participants. The preferred stock accrues dividends at an annual rate of $5.46 per share. At year-end 2005 and 2004, there were 803,953 preferred shares issued and 354,853 and 424,853 shares outstanding, respectively. Each share is convertible at the option of the holder into 4.9625 shares of common stock. The preferred shares may be called by us upon written notice at $78 per share plus accrued and unpaid dividends.

As of December 31, 2005, 0.3 million outstanding shares of preferred stock with a fair value of $104 million and 17 million shares of common stock were held in the accounts of ESOP participants. As of December 25, 2004, 0.4 million outstanding shares of preferred stock with a fair value of $110 million and 18 million shares of common stock were held in the accounts of ESOP participants. Quaker made the final award to its ESOP plan in June 2001.

	2005 Shares	2005 Amount	2004 Shares	2004 Amount	2003 Shares	2003 Amount
Preferred stock	0.8	$41	0.8	$41	0.8	$41
Repurchased preferred stock						
Balance, beginning of year	0.4	$ 90	0.3	$63	0.2	$48
Redemptions	0.1	19	0.1	27	0.1	15
Balance, end of year	0.5	$110*	0.4	$90	0.3	$63

*Does not sum due to rounding.

Note 13 — Accumulated Other Comprehensive Loss

Comprehensive income is a measure of income which includes both net income and other comprehensive income or loss. Other comprehensive loss results from items deferred on the balance sheet in shareholders' equity. Other comprehensive (loss)/income was $(167) million in 2005, $381 million in 2004, and $405 million in 2003. The accumulated balances for each component of other comprehensive loss were as follows:

	2005	2004	2003
Currency translation adjustment	$ (971)	$(720)	$(1,121)
Cash flow hedges, net of tax(a)	27	(19)	(12)
Minimum pension liability adjustment(b)	(138)	(154)	(135)
Unrealized gain on securities, net of tax	31	7	1
Other	(2)	–	–
Accumulated other comprehensive loss	$(1,053)	$(886)	$(1,267)

(a) Includes net commodity gains of $55 million in 2005. Also includes no impact in 2005, $6 million gain in 2004 and $8 million gain in 2003 for our share of our equity investees' accumulated derivative activity. Deferred gains/(losses) reclassified into earnings were $8 million in 2005, $(10) million in 2004 and no impact in 2003.

(b) Net of taxes of $72 million in 2005, $77 million in 2004 and $67 million in 2003. Also, includes $120 million in 2005, $121 million in 2004 and $110 million in 2003 for our share of our equity investees' minimum pension liability adjustments.

Note 14 — Supplemental Financial Information

	2005	2004	2003
Accounts receivable			
Trade receivables	$2,718	$2,505	
Other receivables	618	591	
	3,336	3,096	
Allowance, beginning of year	97	105	$116
Net amounts (credited)/charged to expense	(1)	18	32
Deductions[(a)]	(22)	(25)	(43)
Other[(b)]	1	(1)	–
Allowance, end of year	75	97	$105
Net receivables	$3,261	$2,999	
Inventory[(c)]			
Raw materials	$ 738	$ 665	
Work-in-process	112	156	
Finished goods	843	720	
	$1,693	$1,541	
Accounts payable and other current liabilities			
Accounts payable	$1,799	$1,731	
Accrued marketplace spending	1,383	1,285	
Accrued compensation and benefits	1,062	961	
Dividends payable	431	387	
Insurance accruals	136	131	
Other current liabilities	1,160	1,104	
	$5,971	$5,599	
Other liabilities			
Reserves for income taxes	$1,884	$1,567	
Other	2,439	2,532	
	$4,323	$4,099	
Other supplemental information			
Rent expense	$228	$245	$231
Interest paid	$213	$137	$147
Income taxes paid, net of refunds	$1,258	$1,833	$1,530
Acquisitions[(d)]			
Fair value of assets acquired	$ 1,089	$ 78	$178
Cash paid and debt issued	(1,096)	(64)	(71)
SVE minority interest eliminated	216	–	–
Liabilities assumed	$ 209	$ 14	$107

(a) Includes accounts written off.

(b) Includes collections of previously written-off accounts and currency translation effects.

(c) Inventories are valued at the lower of cost or market. Cost is determined using the average, first-in, first-out (FIFO) or last-in, first-out (LIFO) methods. Approximately 17% in 2005 and 15% in 2004 of the inventory cost was computed using the LIFO method. The differences between LIFO and FIFO methods of valuing these inventories were not material.

(d) In 2005, these amounts include the impact of our acquisition of General Mills, Inc.'s 40.5% ownership interest in SVE for $750 million. The excess of our purchase price over the fair value of net assets acquired is $250 million and is included in goodwill. We also reacquired rights to distribute global brands for $263 million which is included in other nonamortizable intangible assets.

Management's Responsibility for Financial Reporting

To Our Shareholders:

At PepsiCo, our actions — the actions of all our associates — are governed by our Worldwide Code of Conduct. This code is clearly aligned with our stated values — a commitment to sustained growth, through empowered people, operating with responsibility and building trust. Both the code and our core values enable us to operate with integrity — both within the letter and the spirit of the law. Our code of conduct is reinforced consistently at all levels and in all countries. We have maintained strong governance policies and practices for many years.

The management of PepsiCo is responsible for the objectivity and integrity of our consolidated financial statements. The Audit Committee of the Board of Directors has engaged independent registered public accounting firm, KPMG LLP, to audit our consolidated financial statements and they have expressed an unqualified opinion.

We are committed to providing timely, accurate and understandable information to investors. Our commitment encompasses the following:

Maintaining strong controls over financial reporting. Our system of internal control is based on the control criteria framework of the Committee of Sponsoring Organizations of the Treadway Commission published in their report titled, *Internal Control — Integrated Framework*. The system is designed to provide reasonable assurance that transactions are executed as authorized and accurately recorded; that assets are safeguarded; and that accounting records are sufficiently reliable to permit the preparation of financial statements that conform in all material respects with accounting principles generally accepted in the U.S. We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in reports under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the specified time periods. We monitor these internal controls through self-assessments and an ongoing program of internal audits. Our internal controls are reinforced through our Worldwide Code of Conduct, which sets forth our commitment to conduct business with integrity, and within both the letter and the spirit of the law.

Exerting rigorous oversight of the business. We continuously review our business results and strategies. This encompasses financial discipline in our strategic and daily business decisions. Our Executive Committee is actively involved — from understanding strategies and alternatives to reviewing key initiatives and financial performance. The intent is to ensure we remain objective in our assessments, constructively challenge our approach to potential business opportunities and issues, and monitor results and controls.

Engaging strong and effective Corporate Governance from our Board of Directors. We have an active, capable and diligent Board that meets the required standards for independence, and we welcome the Board's oversight as a representative of our shareholders. Our Audit Committee comprises independent directors with the financial literacy, knowledge and experience to provide appropriate oversight. We review our critical accounting policies, financial reporting and internal control matters with them and encourage their direct communication with KPMG LLP, with our General Auditor, and with our General Counsel. In 2005, we named a senior compliance officer to lead and coordinate our compliance policies and practices.

Providing investors with financial results that are complete, transparent and understandable. The consolidated financial statements and financial information included in this report are the responsibility of management. This includes preparing the financial statements in accordance with accounting principles generally accepted in the U.S., which require estimates based on management's best judgment.

PepsiCo has a strong history of doing what's right. We realize that great companies are built on trust, strong ethical standards and principles. Our financial results are delivered from that culture of accountability, and we take responsibility for the quality and accuracy of our financial reporting.

Peter Bridgman

Peter A. Bridgman
Senior Vice President and Controller

Indra K. Nooyi
President and Chief Financial Officer

Steven S Reinemund
Chairman of the Board
and Chief Executive Officer

Management's Report on Internal Control over Financial Reporting

To Our Shareholders:

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) of the Exchange Act. Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based upon the framework in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, our management concluded that our internal control over financial reporting is effective as of December 31, 2005.

KPMG LLP, an independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report and, as part of their audit, has issued their report, included herein, (1) on our management's assessment of the effectiveness of our internal controls over financial reporting and (2) on the effectiveness of our internal control over financial reporting.

Peter Bridgman

Peter A. Bridgman
Senior Vice President and Controller

Indra K. Nooyi
President and Chief Financial Officer

Steven S Reinemund
Chairman of the Board
and Chief Executive Officer

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders PepsiCo, Inc.:

We have audited the accompanying Consolidated Balance Sheet of PepsiCo, Inc. and Subsidiaries as of December 31, 2005 and December 25, 2004 and the related Consolidated Statements of Income, Cash Flows and Common Shareholders' Equity for each of the years in the three-year period ended December 31, 2005. We have also audited management's assessment, included in Management's Report on Internal Control over Financial Reporting, that PepsiCo, Inc. and Subsidiaries maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). PepsiCo, Inc.'s management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on these consolidated financial statements, an opinion on management's assessment, and an opinion on the effectiveness of PepsiCo, Inc.'s internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PepsiCo, Inc. and Subsidiaries as of December 31, 2005 and December 25, 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005, in conformity with United States generally accepted accounting principles. Also, in our opinion, management's assessment that PepsiCo, Inc. maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control — Integrated Framework* issued by COSO. Furthermore, in our opinion, PepsiCo, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control — Integrated Framework* issued by COSO.

KPMG LLP

KPMG LLP
New York, New York
February 24, 2006

Selected Financial Data (in millions except per share amounts, unaudited)

Quarterly	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net revenue				
2005	$6,585	$7,697	$8,184	$10,096
2004	$6,131	$7,070	$7,257	$8,803
Gross profit(a)				
2005	$3,715	$4,383	$4,669	$5,619
2004	$3,466	$4,039	$4,139	$4,943
2005 restructuring charges(b)				
2005	–	–	–	$83
2004 restructuring and impairment charges(c)				
2004	–	–	–	$150
AJCA tax charge(d)				
2005	–	–	$468	$(8)
Net income(e)				
2005	$912	$1,194	$864	$1,108
2004	$804	$1,059	$1,364	$985
Net income per common share — basic(e)				
2005	$0.54	$0.71	$0.52	$0.66
2004	$0.47	$0.62	$0.80	$0.58
Net income per common share — diluted(e)				
2005	$0.53	$0.70	$0.51	$0.65
2004	$0.46	$0.61	$0.79	$0.58
Cash dividends declared per common share				
2005	$0.23	$0.26	$0.26	$0.26
2004	$0.16	$0.23	$0.23	$0.23
2005 stock price per share(f)				
High	$55.71	$57.20	$56.73	$60.34
Low	$51.34	$51.78	$52.07	$53.55
Close	$52.62	$55.52	$54.65	$59.08
2004 stock price per share(f)				
High	$53.00	$55.48	$55.71	$53.00
Low	$45.30	$50.28	$48.41	$47.37
Close	$50.93	$54.95	$50.84	$51.94

The first, second, and third quarters consist of 12 weeks and the fourth quarter consists of 16 weeks in 2004 and 17 weeks in 2005.

(a) Reflects net reclassifications in all periods from cost of sales to selling, general and administrative expenses related to the alignment of certain accounting policies in connection with our ongoing BPT initiative. See Note 1.

(b) The 2005 restructuring charges were $83 million ($55 million or $0.03 per share after-tax). See Note 3.

(c) The 2004 restructuring and impairment charges were $150 million ($96 million or $0.06 per share after-tax). See Note 3.

(d) Represents income tax expense associated with the repatriation of earnings in connection with the AJCA. See Note 5.

(e) Fourth quarter 2004 net income reflects a tax benefit from discontinued operations of $38 million or $0.02 per share. See Note 5.

(f) Represents the composite high and low sales price and quarterly closing prices for one share of PepsiCo common stock.

Five-Year Summary	2005	2004	2003
Net revenue	$32,562	$29,261	$26,971
Income from continuing operations	$4,078	$4,174	$3,568
Net income	$4,078	$4,212	$3,568
Income per common share — basic, continuing operations	$2.43	$2.45	$2.07
Income per common share — diluted, continuing operations	$2.39	$2.41	$2.05
Cash dividends declared per common share	$1.01	$0.850	$0.630
Total assets	$31,727	$27,987	$25,327
Long-term debt	$2,313	$2,397	$1,702
Return on invested capital(a)	22.7%	27.4%	27.5%

Five-Year Summary (Cont.)	2002	2001
Net revenue	$25,112	$23,512
Net income	$3,000	$2,400
Income per common share — basic	$1.69	$1.35
Income per common share — diluted	$1.68	$1.33
Cash dividends declared per common share	$0.595	$0.575
Total assets	$23,474	$21,695
Long-term debt	$2,187	$2,651
Return on invested capital(a)	25.7%	22.1%

(a) Return on invested capital is defined as adjusted net income divided by the sum of average shareholders' equity and average total debt. Adjusted net income is defined as net income plus net interest expense after tax. Net interest expense after tax was $62 million in 2005, $60 million in 2004, $72 million in 2003, $93 million in 2002, and $99 million in 2001.

- As a result of the adoption of SFAS 142, *Goodwill and Other Intangible Assets*, and the consolidation of SVE in 2002, the data provided above is not comparable.
- Includes restructuring and impairment charges of:

	2005	2004	2003	2001
Pre-tax	$83	$150	$147	$31
After-tax	$55	$96	$100	$19
Per share	$0.03	$0.06	$0.06	$0.01

- Includes Quaker merger-related costs of:

	2003	2002	2001
Pre-tax	$59	$224	$356
After-tax	$42	$190	$322
Per share	$0.02	$0.11	$0.18

- The 2005 fiscal year consisted of fifty-three weeks compared to fifty-two weeks in our normal fiscal year. The 53rd week increased 2005 net revenue by an estimated $418 million and net income by an estimated $57 million or $0.03 per share.
- Cash dividends per common share in 2001 are those of pre-merger PepsiCo prior to the effective date of the merger.
- In the fourth quarter of 2004, we reached agreement with the IRS for an open issue related to our discontinued restaurant operations which resulted in a tax benefit of $38 million or $0.02 per share.

Reconciliation of GAAP and Non-GAAP Information

We recognized a tax charge in 2005 related to the Company's intention to repatriate $7.5 billion of international earnings under the provisions of the AJCA. In addition, we recorded restructuring charges in 2005 to reduce costs in some of our operations, principally through headcount reductions, as well as restructuring and impairment charges in 2004 related to Frito Lay's manufacturing consolidation. We also recognized certain tax benefits in 2004. In 2005, we have an additional week of results (53rd week) as our fiscal year ends on the last Saturday of each December, resulting in an additional week of results every five or six years.

The financial measures listed below are not measures defined by generally accepted accounting principles. However, we believe investors should consider these measures as they are more indicative of our ongoing performance. Specifically, investors should consider the following:

- Our 2005 net income and diluted EPS amounts without the impact of the AJCA tax charge, the 53rd week and the restructuring charges, and our 2004 net income and diluted EPS amounts without the impact of prior year tax benefits and restructuring and impairment charges; and
- Our 2005 return on invested capital (ROIC) without the impact of the AJCA tax charge, the restructuring and impairment charges, the 53rd week and prior year tax benefits.

Net Income Reconciliation

Year Ended	2005	2004	Growth
Reported net income	$4,078	$4,212	(3)%
Prior Year Tax Benefits	–	(304)	
AJCA Tax Charge	460	–	
53rd Week	(57)	–	
Restructuring and Impairment Charges	55	96	
Net Income Excluding Prior Year Tax Benefits, AJCA Tax Charge, 53rd Week and Restructuring and Impairment Charges	$4,536	$4,004	13%

Diluted EPS Reconciliation

Year Ended	2005	2004	Growth
Reported diluted EPS	$ 2.39	$ 2.44	(2)%
Prior Year Tax Benefits	–	(0.18)	
AJCA Tax Charge	0.27	–	
53rd Week	(0.03)	–	
Restructuring and Impairment Charges	0.03	0.06	
Net Income Excluding Prior Year Tax Benefits, AJCA Tax Charge, 53rd Week and Restructuring and Impairment Charges	$ 2.66	$ 2.32	15%

ROIC Reconciliation*

Year Ended	2005
Reported ROIC	23%
AJCA Tax Charge	2
ROIC Excluding AJCA Tax Charge	25%

* Impact of restructuring and impairment charges, the 53rd week and prior year tax benefits on ROIC rounds to zero.

Glossary

Anchor bottlers: The Pepsi Bottling Group (PBG), PepsiAmericas, Inc. (PAS) and Pepsi Bottling Ventures (PBV).

Bottler: customers who we have granted exclusive contracts to sell and manufacture certain beverage products bearing our trademarks within a specific geographical area.

Bottler funding: financial incentives we give to our bottlers to assist in the distribution and promotion of our beverage products.

Business Process Transformation (BPT): our comprehensive multi-year effort to drive efficiencies. It includes efforts to physically consolidate, or integrate, key business functions to take advantage of our scale. It also includes moving to a common set of processes that underlie our key activities, and supporting them with common technology application. And finally, it includes our SAP installation, the computer system that will link all of our systems and processes.

Concentrate Shipments and Equivalents (CSE): measure of our physical beverage volume to our customers. This measure is reported on our fiscal year basis.

Consumers: people who eat and drink our products.

Customers: franchise bottlers and independent distributors and retailers.

CSD: carbonated soft drinks.

Derivatives: financial instruments that we use to manage our risk arising from changes in commodity prices, interest rates, foreign exchange rates and stock prices.

Direct-Store-Delivery (DSD): delivery system used by us and our bottlers to deliver snacks and beverages directly to retail stores where our products are merchandised.

Effective net pricing: reflects the year-over-year impact of discrete pricing actions, sales incentive activities and mix resulting from selling varying products in different package sizes and in different countries.

Management operating cash flow: net cash provided by operating activities less capital spending plus sales of property, plant and equipment. It is our primary measure used to monitor cash flow performance.

Marketplace spending: sales incentives offered through various programs to our customers and consumers, as well as advertising and other marketing activities.

Servings: common metric reflecting our consolidated physical unit volume. Our divisions' physical unit measures are converted into servings based on U.S. Food and Drug Administration guidelines for single-serving sizes of our products.

Smart Spot: our initiative that helps consumers find our products that can contribute to healthier lifestyles.

Transaction gains and losses: the impact on our consolidated financial statements of exchange rate changes arising from specific transactions.

Translation adjustments: the impact of the conversion of our foreign affiliates' financial statements to U.S. dollars for the purpose of consolidating our financial statements.

Common Stock Information

Stock Trading Symbol – PEP
Stock Exchange Listings

The New York Stock Exchange is the principal market for PepsiCo common stock, which is also listed on the Amsterdam, Chicago and Swiss Stock Exchanges.

Shareholders

At year-end 2005, there were approximately 197,500 shareholders of record.

Dividend Policy

We target an annual dividend payout of approximately 45% of prior year's net income from continuing operations. Dividends are usually declared in late January or early February, May, July and November and paid at the end of March, June and September and the beginning of January. The dividend record dates for these payments are March 10 and, subject to approval by the Board of Directors, expected to be June 9, September 8 and December 8, 2006. We have paid consecutive quarterly cash dividends since 1965. Amounts in the chart reflect pre-merger PepsiCo for the dates prior to its merger with The Quaker Oats Company.

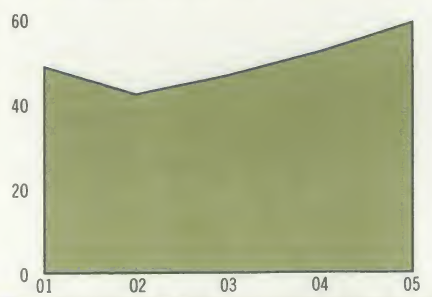
Cash Dividends Declared
Per Share (In $)

Stock Performance

PepsiCo was formed through the 1965 merger of Pepsi-Cola Company and Frito-Lay, Inc. A $1,000 investment in our stock made on December 31, 2000 was worth about $1,284 on December 31, 2005, assuming the reinvestment of dividends into PepsiCo stock. This performance represents a compounded annual growth rate of 5%.

The closing price for a share of PepsiCo common stock on the New York Stock Exchange was the price as reported by Bloomberg for the years ending 2001-2005. These amounts reflect the closing price of pre-merger PepsiCo prior to our merger with The Quaker Oats Company. Past performance is not necessarily indicative of future returns on investments in PepsiCo common stock.

Year-end Market Price of Stock
Based on calendar year-end (In $)



Shareholder Information

Annual Meeting

The Annual Meeting of Shareholders will be held at Frito-Lay Corporate Headquarters, 7701 Legacy Drive, Plano, Texas, on Wednesday, May 3, 2006, at 9 a.m. local time. Proxies for the meeting will be solicited by an independent proxy solicitor. This Annual Report is not part of the proxy solicitation.

Inquiries Regarding Your Stock Holdings

Beneficial Shareholders (shares held by your broker in the name of the brokerage house) should direct communications on all administrative matters to your stockbroker.
Registered Shareholders (shares held by you in your name) should address communications concerning statements, dividend payments, address changes, lost certificates and other administrative matters to:

The Bank of New York
Shareholder Services Department
P.O. Box 11258
Church Street Station
New York, NY 10286-1258
Telephone: 800-226-0083
212-815-3700 (Outside the U.S.)
E-mail: shareowners@bankofny.com
Website: www.stockbny.com
or
Manager Shareholder Relations
PepsiCo, Inc.
700 Anderson Hill Road
Purchase, NY 10577
Telephone: 914-253-3055

In all correspondence or telephone inquiries, please mention PepsiCo, your name as printed on your stock certificate, your Social Security number, your address and telephone number.

SharePower Participants (employees with SharePower options) should address all questions regarding your account, outstanding options or shares received through option exercises to:

Merrill Lynch/SharePower
Stock Option Unit
1600 Merrill Lynch Drive
Mail Stop 06-02-SOP
Pennington, NJ 08534
Telephone: 800-637-6713 (U.S., Puerto Rico and Canada)
609-818-8800 (all other locations)

In all correspondence, please provide your account number (for U.S. citizens, this is your Social Security number), your address, your telephone number and mention PepsiCo SharePower. For telephone inquiries, please have a copy of your most recent statement available.

Employee Benefit Plan Participants

PepsiCo 401(k) Plan & PepsiCo Stock Purchase Program

The PepsiCo Savings & Retirement Center at Fidelity
P.O. Box 770003
Cincinnati, OH 45277-0065
Telephone: 800-632-2014
(Overseas: Dial your country's AT&T Access Number +800-632-2014. In the U.S., access numbers are available by calling 800-331-1140. From anywhere in the world, access numbers are available online at www.att.com/traveler.)
Website: www.netbenefits.fidelity.com

PepsiCo Stock Purchase Program – for Canadian employees:

Fidelity Stock Plan Services
P.O. Box 5000
Cincinnati, OH 45273-8398
Telephone: 800-544-0275
Website: www.iStockPlan.com/ESPP

Please have a copy of your most recent statement available when calling with inquiries.
If using overnight or certified mail send to:

Fidelity Investments
100 Crosby Parkway
Mail Zone KC1F-L
Covington, KY 41015

Shareholder Services

Dividend Reinvestment Plan

A brochure explaining this convenient plan, for which PepsiCo pays all administrative costs, is available on our website www.pepsico.com or from our transfer agent:

The Bank of New York
Dividend Reinvestment Department
P.O. Box 1958
Newark, NJ 07101-9774
Telephone: 800-226-0083

Direct Deposit of Dividends

Information on the Direct Deposit service is available from our transfer agent:

The Bank of New York
Shareholder Services Department
P.O. Box 11258
Church Street Station
New York, NY 10286-1258
Telephone: 800-226-0083
212-815-3700 (Outside the U.S.)

Financial and Other Information

PepsiCo's 2006 quarterly earnings releases are expected to be issued the weeks of April 24, July 10, October 9, 2006, and February 5, 2007.

Copies of PepsiCo's SEC reports, earnings and other financial releases, corporate news and additional company information are available on our website www.pepsico.com.

If you have questions regarding PepsiCo's financial performance contact:

Jamie Caulfield
Vice President, Investor Relations
PepsiCo, Inc.
700 Anderson Hill Road
Purchase, NY 10577
Telephone: 914-253-3035

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New York, NY 10154-0102
Telephone: 212-758-9700

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10:00 AM
PEPSICO
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8:00 AM
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ESSENTIALS
SPORTS
PEPSI
QUAKER
FritoLay
Tropicana